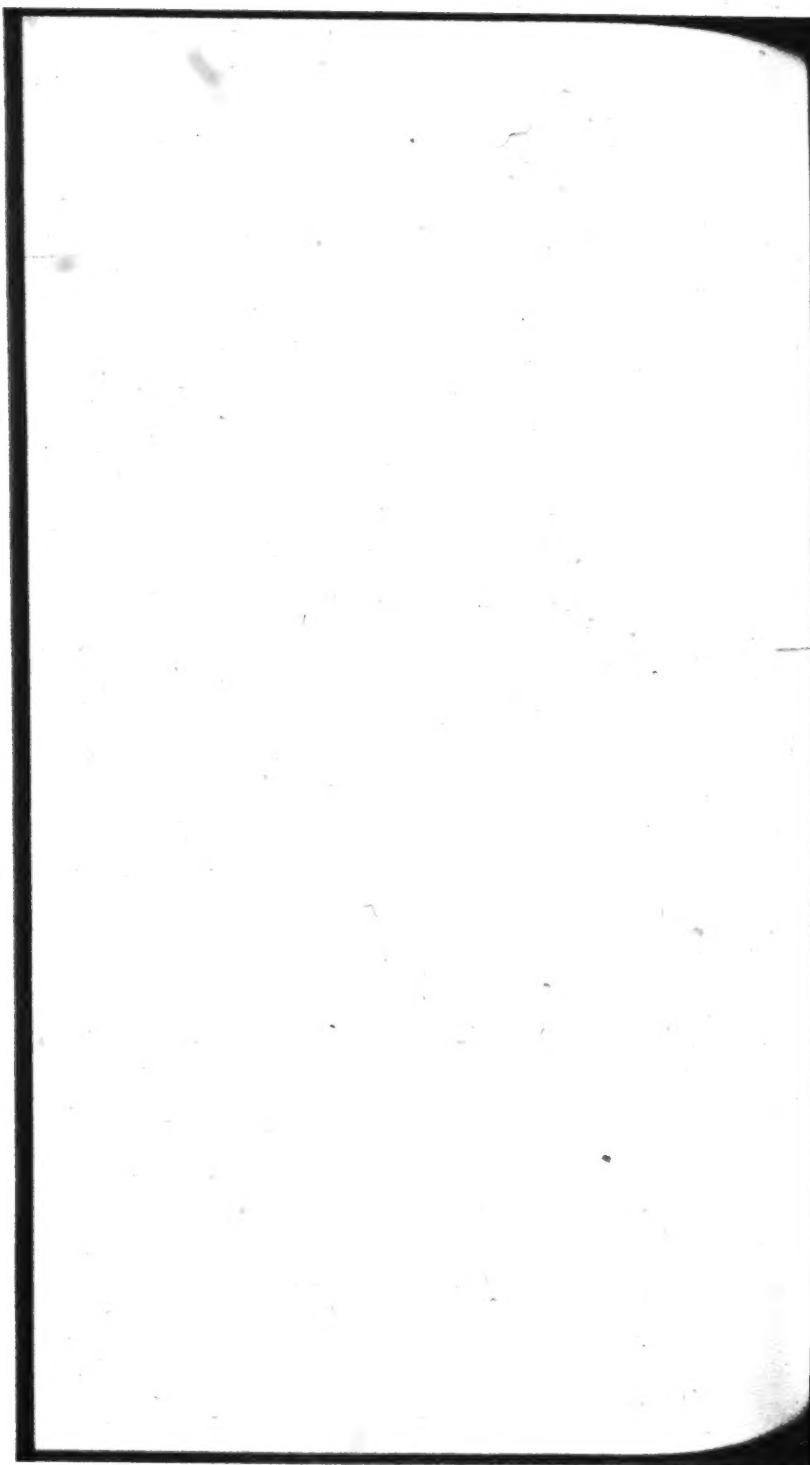


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Appendix.

IN THE

United States District Court

FOR THE NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

No. 70C 3205

GEORGE P. BAKER, RICHARD C. BOND, JERVIS
LANGDON, JR., AND WILLARD WIRTZ, TRUS-
TEES OF THE PROPERTY OF PENN CENTRAL
TRANSPORTATION COMPANY, DEBTOR,

Plaintiffs,

v.

GOLD SEAL LIQUORS, INC.,

Defendant.

DOCKET ENTRIES.

- 12/22/70 Filed Complaint and one copy.
- 12/22/70 Filed designation.
- 12/22/70 Filed Affidavit re Rule 39.
- 12/22/70 Filed Security for Costs.
- 12/23/70 Issued summons and copy with copy of com-
plaint.
- 1/18/71 Filed appearance of defendant and that of its
attorney.

(A1)

- 1/18/71 Filed affidavit under Rule 39.
- 1/21/71 Filed Marshal's return on service of summons returned served.
- 2/16/71 Filed defendant's answer and counterclaim.
- 11/16/71 Filed Stipulation of facts.
- 11/22/71 Filed Plaintiff's Notice; Motion for summary judgment; and Affidavit with copy of order with bankruptcy no. 70-347; and order no. 69 in bankruptcy proceeding, in the Penn Central Transportation Co.
- 11/22/71 Plaintiff given 5 days to file brief in support of motion for summary judgment. Defendant given 20 days to file answer thereof and plaintiff given 5 days thereafter to file reply. Cause taken under advisement.
- NAPOLI, J.
Mailed notices 11/23/71.
- 11/29/71 Filed Memorandum in support of Plaintiff's motion for Summary Judgment.
- 2/16/72 Filed Defendant's Memorandum in opposition to Plaintiff's motion for summary judgment.
- 2/16/72 Leave given to defendant to file instanter memorandum in opposition to plaintiff's motion for summary judgment. Plaintiff given 10 days to reply. Cause set for March 10, 1972 at 1:30 pm for pretrial conference in the chambers of Judge Napoli Room 2156. NAPOLI, J.
Mailed notices 2/17/72.
- 2/25/72 Filed Plaintiffs' Reply to Defendant's Memorandum in Opposition to planitiffs' motion for summary judgment.

- 3/10/72** Pretrial conference held. Motion for summary judgment previously filed herein is taken under advisement.
NAPOLI, J.
Mailed notices 3/13/72.
- 3/16/72** Pursuant to memorandum opinion and order, plaintiffs' motion for summary judgment is granted and judgment is hereby entered in favor of defendant and against plaintiffs in the amount of \$11,017.01. (DRAFT).
NAPOLI, J.
Mailed notices 3/16/72
- 4/10/72** Filed Plaintiff's Notice of filing Notice of Appeal; and Notice of Appeal. pd. \$5.00.
- 4/11/72** Mailed copy of Notice of Appeal to Max W. Petacque and Theodore J. Herst 10 S. LaSalle Chicago, Illinois.
- 4/21/72** Filed Stipulation as to the record on Appeal.

(Title Omitted in Printing)

COMPLAINT.

Now come George P. Baker, Richard C. Bond, Jervis Langdon, Jr. and Willard Wirtz, Trustees of the Property of Penn Central Transportation Company, Debtor, plaintiffs, and complaining against Gold Seal Liquors, Inc., defendant, states as follows:

1. This action arises under the laws of the United States regulating commerce, 49 U.S.C. §§ 3(2) and 6(7). This Court has jurisdiction of this action under 28 U.S.C. § 1337.

2. Penn Central Transportation Company is a corporation organized under the laws of the State of Pennsylvania and is a common carrier by railroad subject to the provisions of the Interstate Commerce Act, 49 U.S.C. § 1 et seq.

3. Defendant is a corporation doing business in the Northern District of Illinois.

4. During the period August 22, 1968 to and including June 18, 1970 plaintiffs received and transported for defendant's account various consignments of alcoholic liquors.

5. Pursuant to the charges provided in the lawfully published tariffs filed by plaintiffs with the Interstate Commerce Commission, there is due and owing from defendant to plaintiffs unpaid freight charges in the amount of Eight Thousand Two Hundred Fifty-Six and 61/100 (\$8,256.61) Dollars for the transportation of the consignments described in paragraph 4 above.

6. The dates, waybill numbers, car numbers and freight charges pertaining to the individual shipments are set forth in Appendix A attached to the complaint.

7. Defendant has refused to pay the above lawfully described charges although payment was duly demanded.

WHEREFORE, plaintiffs pray judgment against defendant in the amount of Eight Thousand Two Hundred Fifty-Six and 61/100 (\$8,256.61) Dollars together with interest and costs of suit.

GEORGE P. BAKER, RICHARD C. BOND,
JERVIS LANGDON, JR. AND WILLARD
WIRTZ, TRUSTEES OF THE PROPERTY
OF PENN CENTRAL TRANSPORTATION
COMPANY, DEBTOR,

Plaintiffs.

By EDWARD R. GUSTAFSON,
Edward R. Gustafson,

Attorney.

532 Union Station
Chicago, Illinois 60606
Phone: CEntal 6-7200 Ext. 2641

Appendix "A".

GOLD SEAL LIQUORS.

Subject:	<u>Waybill No.</u>	<u>Date</u>	<u>Car No.</u>	<u>Amount</u>
	19520	08/22/68	706222	\$ 93.50
	19708	05/10/69	370156	606.00
	229430	07/26/69	707028	41.00
	19696	06/24/69	100369	40.93
	19726	12/09/69	472358	658.60
	223124	12/08/69	201792	265.95
	19767	12/16/69	479353	640.00
	19785	12/17/69	303541	645.80
	229149	12/23/69	200209	456.75
	19799	12/18/69	478384	642.00
	19806	12/30/69	101062	658.40
	19782	12/29/69	500355	652.80
	19791	12/18/69	250378	640.00
	19852	12/29/69	100460	640.00
	229547	11/08/69	370220	206.55
	229088	12/12/69	700682	249.30
	19750	12/10/69	152274	340.38
	229620	11/13/69	207279	45.71
	229013	06/18/70	30811	392.94
				<hr/>
				\$8,256.61

(Title Omitted in Printing)

ANSWER AND COUNTERCLAIM

ANSWER.

Now COMES, Gold Seal Liquors, Inc., an Illinois corporation, answering the complaint of the plaintiff and states as follows:

1. Defendant admits the allegations of Paragraph 1 of said complaint.

2. Defendant admits the allegations of Paragraph 2 of said complaint.

3. Defendant admits the allegations of Paragraph 3 of said complaint.

4. Defendant admits that for some time prior to and during the period August 22, 1968, to and including June 18, 1970, Penn Central Transportation Company, a Pennsylvania corporation, later known as Penn Central, received for defendant's account alcoholic beverages.

5. Defendant denies the allegations in Paragraph 5 of said complaint.

6. Defendant denies that Exhibit "A" correctly states or reflects the liability of defendant thereunder.

7. Defendant denies that it is indebted to plaintiffs in the sum of \$8,256.61 or any sum whatsoever.

COUNTERCLAIM.

Defendant, Gold Seal Liquors, Inc., for its counterclaim against plaintiffs states as follows:

1. Jurisdiction of this cause is founded on 28 U. S. C. §§ 1332 and 1337. Plaintiffs and defendant are citizens of different states and the amount in controversy exceeds \$10,000.00, exclusive of interest and costs.

2. Penn Central Transportation Company is a corporation organized under the laws of the State of Pennsylvania and is a common carrier by railroad subject to the provisions of the Interstate Commerce Act, 49 U. S. C. § 1 et seq.

3. Defendant is an Illinois corporation doing business in the Northern District of Illinois.

4. During the period August 22, 1968, to and including June 18, 1970, both inclusive, Penn-Central shipped to defendant in Penn-Central trailers carried on Penn-Central flat cars, alcoholic beverages from company plants and warehouses, which were received by defendant at defendant's warehouse in Chicago, Illinois, in damaged condition, caused by theft or breakage, or both, as a result of plaintiff's lack of care and breach of its contract of carriage enroute. Defendant has paid the freight charges thereon and complying with the terms of the bills of lading and the procedures prescribed by the railroad and under the regulations of the Interstate Commerce Commission, and pursuant to the statute in such case made and provided, filed claims for said damage to said shipments in apt time. The aggregate amount of the damaged merchandise for which defendant filed claims for reimbursement is \$19,319.42. The date of each claim filed and the amount thereof are set forth on Exhibit "A" attached hereto and made a part hereof.

5. Although frequently requested so to do, plaintiffs have failed and refused to pay said sum or any part thereof. To defendant's damage in the sum of \$19,319.42.

WHEREFORE, defendant, Gold Seal Liquors, Inc., prays judgment against plaintiffs, George P. Baker, Richard C. Bond, Jervis Langdon, Jr. and Willard Wirtz, Trustees of the Property of Penn Central Transportation Company,

dismissing plaintiffs' complaint and that defendant have and recover judgment against plaintiffs for \$19,319.42, together with the costs of this action. Defendant demands trial by jury.

GOLD SEAL LIQUORS, INC.,

By MAX W. PETACQUE,

By THEODORE J. HERST,

Attorneys for Defendant.

10 S. LaSalle St., Chicago, Ill.,
263-5600.

Answer and Counterclaim

CLAIMS OF GOLD SEAL LIQUORS, INC.
FILED AGAINST PENN CENTRAL RAILROAD.

<u>Date of Filing</u>	<u>Amount</u>
12/12/68	\$ 417.00
3/ 7/69	2,720.57
6/30/69	1,023.36
7/31/69	1,807.00
9/30/69	1,186.03
9/24/69	690.67
10/31/69	1,655.50
10/23/69	336.93
11/10/69	619.03
11/20/69	20.00
11/28/69	660.94
11/28/69	1,844.36
11/28/69	802.10
12/16/69	1,204.68
12/16/69	884.71
12/31/69	2,862.87
4/30/70	29.51
4/30/70	21.98
5/28/70	72.14
5/28/70	210.39
6/15/70	249.65
	<hr/>
	\$19,319.42

(Title Omitted in Printing)

STIPULATION OF FACTS.

It is hereby stipulated and agreed by and between the parties hereto by their respective counsel of record that the following facts are admitted and agreed upon by the parties and shall be taken as true without any evidence being produced thereon:

1. This action arises under the laws of the United States regulating commerce, 49 U. S. C. §§ 3(2) and 6(7). This Court has jurisdiction of this action under 28 U. S. C. § 1337.

2. Penn Central Transportation Company is a corporation organized under the laws of the State of Pennsylvania and is a common carrier by railroad subject to the provisions of the Interstate Commerce Act, 49 U. S. C. § 1 et seq.

3. Defendant is a corporation doing business in the Northern District of Illinois.

4. During the period August 22, 1968 to and including June 18, 1970, plaintiffs received and transported for defendant's account various consignments of alcoholic liquors.

5. There is due and owing from defendant to plaintiff transportation charges as follows:

Stipulation of Facts

<u>Waybill No.</u>	<u>Car No.</u>	<u>Amount Owing By Defendant</u>
19708	370156	557.52
19726	472358	658.60
223124	201792	265.95
19767	479353	340.00
19785	303541	645.80
229149	200209	456.75
19799	478384	642.00
19806	101062	658.40
19782	500355	652.80
19791	250378	640.00
19852	100460	640.00
229547	370220	206.55
229088	700682	249.30
19750	152274	340.38
229620	207279	45.71
		<hr/>
		\$6,999.76

6. Defendant has filed a counterclaim listing alleged claims for loss and damage with plaintiff, which claims are alleged to be as follows:

Stipulation of Facts

A13

	<u>Date of Filing</u>	<u>Amount</u>
9854	12/12/68	\$ 417.00
B253	3/7/69	2,720.57
B667	6/30/69	1,023.36
B791	7/31/69	1,807.00
B999	9/30/69	1,186.03
B1053	9/24/69	690.67
B1142	10/31/69	1,655.50
B1182	10/23/69	366.93
B1326	11/10/69	619.03
B1355	11/20/69	20.00
B1361	11/28/69	660.94
B1364	11/28/69	1,844.36
B1366	11/28/69	802.10
B1457	12/16/69	1,204.68
B1458	12/16/69	884.71
B1593	12/31/69	2,862.87
B2148	4/30/70	29.51
B2149	4/30/70	21.98
B2271	5/28/70	72.14
B2272	5/28/70	210.39
B2492	6/15/70	249.65
		<hr/>
		\$19,319.42

Of the aforesaid claims for loss and damage plaintiff has admitted that all are valid in the amount shown except as follows:

<u>Claim No.</u>	<u>Amount</u>	<u>Status</u>
B1182	\$ 336.93	Disallowed
B1355	20.00	No record
B1593	2,862.87	No record
	<hr/>	
	\$3,219.80	

Stipulation of Facts

In addition to the aforesaid amounts, plaintiff has admitted the existence of further valid claims of defendant as follows:

<u>Claim No.</u>	<u>Amount</u>
2515	\$ 649.00
B2460	244.79
BLNZ0000206141	1,023.36
	<hr/>
	\$1,917.15

Thus, the total amount which plaintiff admits being indebted to defendant by virtue of valid claims filed with it is \$18,016.77.

7. As to said claims filed by defendant in the sum of \$19,319.42, which sum includes claims aggregating \$18,016.77, which plaintiff admits to be valid and owing to defendant; defendant, in establishing said claims, has paid the freight charges therein, has complied with the terms of the bills of lading therefor and the procedures prescribed by plaintiff and to the requirements of the Interstate Commerce Commission and the applicable statutes pertaining thereto, and has filed its said claims for damages in apt time.

8. Pursuant to Order No. 164, entered February 17, 1971, in the reorganization proceedings now pending in the United States District Court for the Eastern District of Pennsylvania entitled "In the Matter of Penn Central Transportation Company, Debtor, In Proceedings for Reorganization of a Railroad, No. 70-347," a Proof of Claim has been recorded as having been filed for defendant

for freight loss or damage in the sum of \$19,631.76, representing \$17,588.48, approved, but not paid, and \$2,042.78 under investigation.

GEORGE P. BAKER, RICHARD C. BOND,
JERVIS LANGDON, JR. and WILLARD
WIRTZ, TRUSTEES OF THE PROPERTY
OF PENN CENTRAL TRANSPORTATION
COMPANY, DEBTOR.

By EDWARD B. GUSTAFSON,
Attorney.

GOLD SEAL LIQUORS, INC.

By THEODORE J. HERST,
One of its Attorneys.

(Title Omitted in Printing)

MOTION FOR SUMMARY JUDGMENT.

Plaintiff, Penn Central Transportation Company, by its attorney, Edward R. Gustafson, moves this Court to enter, pursuant to Federal Rule of Civil Procedure 56(b), summary judgment in said plaintiff's favor and against defendant, Gold Seal Liquors, Inc., in the amount of \$6,999.76 together with interest and costs and, in support thereof, states:

1. The complaint filed in this proceeding alleges that there is due and owing to plaintiff from defendant the sum of \$8,256.61 for unpaid freight charges for transportation performed by plaintiff for and on behalf of defendant during the period August 22, 1968 to and including June 18, 1970.

With respect to the charges alleged to be due, defendant has admitted that said charges are correct in some respects but incorrect in others. The waybill numbers, car numbers, amounts claimed to be due by plaintiff and amounts admitted to be due by defendant, are listed in the stipulation of facts heretofore filed herein. As indicated in said stipulation, amounts admitted to be due and owing by defendant to plaintiff aggregate \$6,999.76.

2. Defendant has filed a counterclaim in this proceeding alleging loss and damage to various shipments of merchandise handled by plaintiff for defendant's account. The claim numbers and amounts thereof are set forth in the stipulation in the total amount of \$19,319.42. Of this

amount plaintiff has admitted the validity of claims aggregating \$18,016.77. The claim numbers, and their amounts, which plaintiff has allowed, disallowed, or has no record of, are set forth in the stipulation.

3. As indicated in the affidavit attached hereto, George P. Baker, Richard C. Bond, Jervis Langdon, Jr. and Willard Wirtz, the petitioners, are trustees of the Penn Central Transportation Company, Debtor. They were appointed on July 22, 1970 by the District Court of the United States for the Eastern District Court of the United States for the Eastern District of Pennsylvania in cause #70-347 with the powers of a trustee under Section 44 of the Bankruptcy Act and the powers of the receiver to operate the business of the Penn Central Transportation Company as a common carrier by railroad engaged in interstate commerce and is licensed to transact business in the State of Illinois. The initial order of the Bankruptcy Court, dated June 21, 1970, approving the petition of the Debtor and making various authorizations and directions is attached hereto.

4. Plaintiff alleges that it is entitled to judgment against defendant in the amount of \$6,999.76 and that defendant is entitled to judgment against plaintiff in the amount of \$18,016.77. Plaintiff contends, however, that the law pertaining to the reorganization of a railroad does not permit an offset or set off of one claim against the other resulting in a net judgment for defendant.

5. The affidavit of Edward R. Gustafson is attached hereto.

WHEREFORE, plaintiff moves that it have judgment against defendant in the amount of \$6,999.76 and that de-

Motion for Summary Judgment

defendant have judgment against plaintiff in the amount of \$18,016.77.

GEORGE P. BAKER, RICHARD C. BOND,
JERVIS LANGDON, JR. AND WILLARD
WHITE, TRUSTEES OF THE PROPERTY
OF PENN CENTRAL TRANSPORTATION
COMPANY, DEBTOR,

Plaintiff.

By: EDWARD R. GUSTAFSON.
Edward R. Gustafson.

Edward R. Gustafson,
Attorney for Plaintiff.
532 Union Station,
Chicago, Illinois 60606
Central 6-7200, Ext. 2641

(Title Omitted in Printing)

STATE OF ILLINOIS }
COUNTY OF COOK } ss.:

AFFIDAVIT.

Edward R. Gustafson, who is Assistant General Attorney of the Penn Central Transportation Company, and whose address is Room 532 Union Station, 516 W. Jackson Blvd., Chicago, Ill., 60606, being duly sworn, deposes and says that:

1. George P. Baker, Richard C. Bond, Jervis Langdon, Jr. and Willard Wirtz, the petitioners are trustees of the Penn Central Transportation Company, Debtor. They were appointed on July 22, 1970 by the District Court of the United States for the Eastern District Court of the United States for the Eastern District of Pennsylvania in cause #70-347 with the powers of a trustee under Section 44 of the Bankruptcy Act and the powers of the receiver to operate the business of the Penn Central Transportation Company as a common carrier by railroad engaged in interstate commerce and is licensed to transact business in the State of Illinois. The initial order of the Bankruptcy Court, dated June 21, 1970, approving the petition of the Debtor and making various authorizations and directions is attached hereto.

2. The Penn Central System comprises 21.4% of the miles of road operated by the railroads of the United States and 42.3% of the miles of road in the eastern district.

3. Penn Central Transportation Company in 1969 handled 11.3% of the tonnage of freight moved by railroads in the United States and 26.3% of the freight tonnage in the eastern district.

4. Penn Central Transportation Company revenues comprise 14.4% of the revenues of the class 1 railroads in the United States and 34% of the revenue in the eastern district.

5. The Penn Central Transportation Company serves 86,000 shippers.

6. The class 1 railroads of the United States provided the movement of 780,000,000 freight ton-miles of service in 1969, which is 41% of the intercity freight ton-miles moved in the United States. Trucks moved 21.2% in terms of ton-miles, and other modes of transportation (pipeline, barge, etc.) moved 37.8%. Of the total freight ton-miles of service provided by the United States railroads, Penn Central Transportation Company provided 11.5%, and of the total provided by the railroads in the eastern district, Penn Central Transportation Company provided 34%.

7. Penn Central under the guidance of the Trustees has materially improved its service to the point that complaints from shippers about service deficiencies have dropped 94%. However, the railroad operation continues to register a very substantial deficit and the Trustees predict that cash made available from Government guarantees will be exhausted and if the operation is to continue further cash will be required from some source by the first quarter of 1972. In the meanwhile, freight traffic has fallen off due to the general economic slow down (3.8% during the first half of 1971 below the 1970 figure with a greater decline [over 8%] during the last few weeks). The mineworkers' walkout and the longshoremen's strike have caused serious loss of traffic. While some progress toward viability has been made, if these trends continue the future is unpredictable.

8. In the reorganization proceedings, the proof of claim procedure has resulted in the filing of 9600 claims for loss and damage in the amount of \$29,600,000. Of accounts

receivable, about 55,000 items totaling \$59,200,000 are past due in the sense that they are older than 90 days. At the time Penn Central Transportation Company went into reorganization on June 21, 1970, such past due accounts receivable totaled \$28,000,000.

9. The facts stated herein are true and correct to the best of his knowledge and belief.

EDWARD R. GUSTAFSON.

Subscribed and sworn to before me this 17th day of November, 1971.

MARIE M. MARSHALL
Notary Public

IN THE
DISTRICT COURT OF THE UNITED STATES
FOR THE EASTERN DISTRICT OF PENNSYLVANIA

IN PROCEEDINGS FOR THE REORGANIZATION OF A RAILROAD

No. 70-347

In The Matter Of

PENN CENTRAL TRANSPORTATION COMPANY,
Debtor.

ORDER.

Upon due consideration of the petition of Penn Central Transportation Company, the above named Debtor, verified June 21, 1970 and filed herein this day, and the Court being satisfied that such petition complies with Section 77 of the Bankruptcy Act (11 U.S.C. Sec. 205) and has been filed in good faith, it is ORDERED:

1. Said petition be, and it hereby is, approved as properly filed under said Section 77 of the Bankruptcy Act (11 U.S.C. Sec. 205).

2. The Debtor shall be, and it hereby is, authorized and directed, pending further order of this Court, to run, manage, operate, maintain, preserve and keep in proper condition and repair the railroad and properties, including leased railroads and property, of the Debtor wherever situated, whether in this State, judicial district, or elsewhere; to manage, operate and conduct its business,

and to this end to exercise its authority, rights and franchises and to discharge its public duties; to employ and discharge and fix the compensation of, all officers, agents, employees and counsel; to continue any existing arrangements or otherwise arrange with others for rendering services to the Debtor or for the payment of expenses incurred by others on behalf of or for the account of the Debtor in connection with the management, operation and conduct of the Debtor's railroad, properties and business including, without limitation, executive, supervisory, accounting, financial, engineering, operating, real estate, purchasing, insurance, tax and administrative services, and to fix and pay the compensation therefor whether on a basis of reimbursement of charges actually incurred or otherwise; to collect and receive the income, rents, revenues, tolls, issues and profits, accrued or to accrue, from its railroad and properties; to collect all outstanding interline and other accounts owing to the Debtor, and all dividends and interest on securities belonging to it; to sell, convey or lease property of the Debtor, real or personal, not needed in the operation of its railroad, and to exercise such rights of sale, conveyance, exchange and release as are reserved to, or available to, the Debtor under its outstanding deeds of trust, mortgages, trust indentures, and similar instruments, and to use, or cause to be applied, the proceeds of sale of released property as provided in such instruments, all in the same manner that the Debtor would be entitled to do in its own right; to the extent necessary to protect or preserve its railroad, or properties or business, to make and pay for additions, betterments and improvements thereto and thereof; to perform its existing contracts made in the regular course of business to the extent that performance thereof may seem desirable, but such performance shall not constitute an

affirmance of said contracts or any thereof; and to enter into and perform other contracts in the regular course of the conduct of its business; all to the end that the business of the Debtor may be continued, operated and managed according to the customary and usual manner of conducting the same, and all of the foregoing powers to be exercised by the Debtor according to law and subject to such supervision and control by the Court as the Court may exercise by further orders entered herein.

3. The Debtor is authorized in its discretion, from time to time until the further order of this Court, out of funds now in its possession or hereafter coming into its hands, to pay all or any of the following, in whole or in part, without limiting the generality thereof, and to adjust or compromise the same:

A. Taxes, assessments and other governmental charges now due or hereafter coming due upon or measured by, the properties, pay-rolls, income, franchises or business of the Debtor;

B. All other current expenses and costs hereafter necessarily incurred in operating, maintaining and preserving its railroad and other properties, collecting the revenues, and conducting the business of the Debtor, whether or not chargeable to operating expenses under applicable accounting rules; including, without limitation, all wages, salaries and compensation of officers, agents, employees, consultants and counsel employed or retained by the Debtor, all inter-line accounts and balances owing by Debtor, including amounts in respect of revenues from freight, passenger or other traffic interchanged with other carriers, and charges for repairs of, or loss or damage to, rolling stock and equipment interchanged with

other carriers, all claims for injuries, death or other loss or damage to passengers and others arising from the operation of its railroad and properties, and all claims for loss, damage or delay to freight and baggage, and all claims for overcharges and for reparation, and all accounts for services, materials and supplies rendered or furnished to the Debtor, whether chargeable in the first instance to expenses, or otherwise; provided, that any of the foregoing accounts and claims may, in the discretion of the Debtor, either be paid in full or adjusted or compromised;

C. All amounts hereafter coming due, whether as rent, car hire, per diem, mileage or otherwise, in respect of the use or possession by the Debtor of locomotives, cars and other rolling stock and equipment, including the principal of, and interest or dividends on, equipment obligations issued, guaranteed or assumed by the Debtor; and all amounts hereafter coming due under any lease, joint facility contract, or other contract or agreement, for or in respect of the occupation or use by the Debtor, whether solely or jointly, of lines of railroad, terminals, docks, piers, tracks, buildings, depots, sidetracks, yards, warehouses, shops, bridges, interlocking plants and other railroad property and facilities; provided, however, that no such payment or payments shall constitute an affirmation or adoption of said leases, joint-facility contracts or other contracts or agreements, or any of them;

D. All liabilities and costs hereafter coming due in respect of the construction or acquisition of property or work heretofore authorized and actually initiated or contracted for by the Debtor and constituting additions, betterments or improvements of any railroad property of or used by the Debtor; but, with-

out further order of this Court, no expenditure shall be made for any acquisition, construction or work constituting an addition, betterment or improvement, not heretofore authorized and actually initiated or contracted for by the Debtor, except for additions, betterments and improvements necessarily incident to the current maintenance and preservation of the Debtor's railroad and properties;

E. All claims, liabilities and costs of the characters specified in the foregoing paragraphs B, C and D of this order incurred by the Debtor and coming due within six months preceding the date of this order in the usual and customary operation of its railroad and properties and the conduct of its business; provided, however, that no payment shall, without the further order of this Court, be made under paragraph E in respect of any additions, betterments and improvements not necessarily incident to the current maintenance and preservation of the Debtor's property, and provided, further that no liability or cost coming due more than six months preceding the date of this order shall be paid by the Debtor without the further order of this Court; except as provided in paragraphs A and F of this order;

F. All outstanding checks or vouchers for wages, salaries or other compensation for services, regardless of when issued; and all claims preferred under Section 77(n) of the Bankruptcy Act (11 U.S.C. Sec. 205(n)), regardless of when accrued or of the time of presentation or assertion thereof, but any such claims may be paid in full, or adjusted or compromised by the Debtor, in its discretion;

G. The cost of maintaining the corporate existence of the Debtor, including corporate, franchise, stamp

and similar taxes, such office rent and relocation of offices as may be required, and the necessary expense of keeping and preserving its corporate records, of maintaining offices and agencies for transferring and registering its stock and bonds, and the proper charges and expenses of trustees under indentures or mortgages pursuant to which securities of, or assumed or guaranteed by, the Debtor have been issued;

H. All payments due from time to time on established retirement and compensation arrangements, and all group insurance carried in whole or in part by the Debtor;

I. Court costs and costs incurred before various State and Federal Commissions or other administrative boards or tribunals; and

J. The expense of printing pleadings, motions, petitions, orders and other documents now on file or hereafter filed in this proceeding, reasonably necessary to be printed, in such quantity as shall provide copies for the use of the Court, the Interstate Commerce Commission, the Debtor, parties to the cause and such others as may have any interest therein, such expense to be taxed as costs in this proceeding.

Until the further order of this Court, no payment shall be made by the Debtor upon or in respect of the principal of, or interest on, any of its funded or floating debt, except the principal of, and interest or dividends on, equipment obligations issued, guaranteed or assumed by the Debtor.

4. The Debtor shall have the power to elect whether to adopt or continue in force, or to refuse to adopt or continue in force or to disaffirm or reject, any lease, trackage, terminal, crossing or operating agreement, or

other contract not fully performed to which it is a party or under which it may be obligated; and the Debtor, or the trustee or trustees hereafter appointed and qualified, shall be allowed a period of six months (or such further period as this Court may allow) from the date of the entry of this order to make such election. Such elections may be made from time to time, and any such election shall be made by instrument in writing, signed by the duly authorized officer or officers of the Debtor, or by such trustees of the property of the Debtor as may hereafter be appointed and qualify, and delivered, or mailed by registered mail, postage prepaid, addressed to the other party or parties to said lease, agreement or contract; and any such election shall be effective when a copy of such instrument, together with proof of delivery or mailing of a copy or copies thereof as aforesaid to the other party or parties to such lease, agreement or contract shall be filed of record in this proceeding. No occupancy, conduct or user of property or rights by the Debtor, or payments made by the Debtor as rent or otherwise or accepted by it as rent or otherwise, or any other acts or omissions by the Debtor during said period (or such other period as this Court may allow), except an instrument filed and delivered or mailed as aforesaid expressly electing to adopt any such lease, agreement or contract shall be deemed to preclude or conclude the Debtor in respect of such election or be deemed to constitute an election to adopt or continue in force any such lease, agreement or contract. In case payments are made pursuant to the foregoing authority contained in Subdivision C of paragraph 3 hereof and any such leases, agreements or contracts shall be subsequently adopted by the Debtor, or such trustee or trustees of the property of the Debtor as may hereafter be appointed and qualify, or pursuant to a plan of reorganization, said payments shall be deemed to have been made on account of

the rental due from the Debtor under such leases, agreements or contracts. In case any such lease, agreement or contract shall be disaffirmed or rejected by the Debtor, or by such trustee or trustees, or under a plan of reorganization, the operation of the leased or used properties shall be deemed to have been, and such payments to have been made, for the account of the lessors or owners, respectively, and such payments shall be recovered, set off, or made and charged, on the earnings or properties, or both, of the respective lessor or owner, as the case may be, prior to any mortgage or other lien thereon, by such method as the Court shall determine; and all rights and equities of the parties arising from such payments shall be reserved for later determination.

5. Pending further order of the Court, the Debtor is authorized and empowered to institute or prosecute in any court or before any tribunal of competent jurisdiction all such suits and proceedings as may be necessary in its judgment for the recovery or proper protection of its property or rights, and to liquidate, compromise, adjust or make settlement, by written agreement or consent judgment or otherwise, of any thereof; and likewise to defend and to liquidate, compromise, adjust or make settlement of any actions, proceedings or suits now pending against the Debtor or which may hereafter be asserted or be brought in any court or before any officer, department, commission or tribunal to which the Debtor is or shall be a party; but no payment shall, without further order of this Court, be made by the Debtor in respect of any such actions, proceedings or suits on claims accruing prior to the date of this order, except such claims as may be permitted to be paid by this order or by other general orders hereafter entered herein, and such as constitute preferred claims under the Acts of Congress relating to bankruptcy; and no action

taken by the Debtor in defense or settlement of such claims, actions, proceedings or suits shall have the effect of establishing any claim upon, or right in, the property or funds in the possession of the Debtor that otherwise would not exist.

6. The Debtor shall close its present books of account as of midnight on June 21, 1970, and shall open new books of account as of 12:01 A.M. E.D.S.T. on June 22, 1970, and cause to be kept therein due and proper accounts of the earnings, expenses, receipts and disbursements of the Debtor, and shall preserve proper vouchers for all payments made by the Debtor, and shall deposit the monies coming into its hands in the banks in which funds of the Debtor are presently deposited, or such thereof as shall be selected by the Debtor, or in such other bank or banks as shall be selected by the Debtor.

7. Depositories of Debtor's funds be and each of them hereby is authorized to honor all checks, drafts and vouchers drawn by Debtor against its account or accounts and to carry on similar banking transactions with the Debtor without regard to the fact that the petition of the Debtor heretofore filed under Section 77 of the Acts of Congress relating to bankruptcy has been approved by this Court.

8. Not later than August 17, 1970, unless the time be extended by further order of this Court, the Debtor shall file with the Clerk of this Court a statement of the assets and liabilities of the Debtor as of the close of business on June 21, 1970, and within 60 days after the close of each calendar month thereafter shall file with said Clerk a statement of the assets and liabilities of the Debtor as of the close of business on the last day of such calendar month, together with a summary statement of the revenues and

expenses of the Debtor, for such calendar month. All such statements shall be certified as correct by the chief accounting officer of the Debtor.

9. All persons and all firms and corporations, whatsoever and wheresoever situated, located or domiciled, hereby are restrained and enjoined from interfering with, seizing, converting, appropriating, attaching, garnisheeing, levying upon, or enforcing liens upon, or in any manner whatsoever disturbing any portion of the assets, goods, money, deposit balances, credits, choses in action, interests, railroads, properties or premises belonging to, or in the possession of the Debtor as owner, lessee or otherwise, or from taking possession of or from entering upon, or in any way interfering with the same, or any part thereof, or from interfering in any manner with the operation of said railroads, properties or premises or the carrying on of its business by the Debtor under the order of this Court and from commencing or continuing any proceeding against the Debtor, whether for obtaining or for the enforcement of any judgment or decree or for any other purpose, provided that suits or claims for damages caused by the operation of trains, buses, or other means of transportation may be filed and prosecuted to judgment in any Court of competent jurisdiction, and provided, further, that the title of any owner, whether as trustee or otherwise, to rolling stock equipment leased or conditionally sold to the Debtor, and any right of such owner to take possession of such property in compliance with the provisions of any such lease or conditional sale contract, shall not be affected by the provisions of this order.

10. All persons, firms and corporations, holding collateral heretofore pledged by the Debtor as security for its notes or obligations or holding for the account of the Debtor deposit balances or credits be and each of them

hereby are restrained and enjoined from selling, converting or otherwise disposing of such collateral, deposit balances or other credits, or any part thereof, or from offsetting the same, or any thereof, against any obligation of the Debtor, until further order of this Court.

11. The Debtor hereby is directed to give notice by mailing a copy of this order to the trustee or trustees under each mortgage or other indenture pursuant to which any securities of, or assumed or guaranteed by, the Debtor, have been issued, and to cause a notice, directed to its creditors and stockholders, to be published within five days from the date of the entry of this order, once each in the *Evening Bulletin* and the *Philadelphia Inquirer*, newspapers published in the City of Philadelphia, State of Pennsylvania, once in *The New York Times* and the *Wall Street Journal*, newspapers published in the City of New York, State of New York, and in the *Chicago Tribune*, a newspaper published in the City of Chicago, State of Illinois, of a hearing to be held on July 15, 1970, at 11:00 o'clock A.M., in Court Room No. 3 of this Court in the United States Court House, Ninth and Market Streets, Philadelphia, Pennsylvania, at which hearing or any adjournment thereof this Court will appoint one or more trustees of the Debtor's property. The notice of such hearing shall be substantially in the form of the notice annexed hereto, made a part hereof and designated "Exhibit A." When such mailing and publication have been completed the Debtor shall file with the Clerk of this Court its sworn report with respect thereto.

12. This Court reserves full right and jurisdiction to make, from time to time, such orders as the Court shall deem proper limiting the time within which suits against the Debtor may be brought, staying any suits now pending or hereafter brought against the Debtor, appointing a trustee or trustees of all of said Debtor's property and estate,

with all the title and powers of such trustee or trustees under and subject to the provisions of the Acts of Congress relating to bankruptcy, including the power to operate the business of the Debtor, fixing the time within which any plan of reorganization shall be proposed, accepted and confirmed, requiring the Debtor to file such schedules and submit such information as may be necessary to disclose the conduct of the Debtor's affairs and the fairness of any proposed plan, fixing a reasonable time within which claims and interests of creditors and stockholders may be filed or evidenced and allowed, and the division of creditors and stockholders into classes according to the nature of their respective claims and interests and, in general, such orders amplifying, extending, supplementing, limiting or otherwise modifying this order as to the Court may at any time seem proper.

C. WILLIAM KRAFT, JR.,
U. S. District Judge.

June 21, 1970.

Exhibit "A"

**NOTICE TO ALL CREDITORS AND
STOCKHOLDERS OF THE
PENN CENTRAL TRANSPORTATION COMPANY**

Pursuant to an order entered June 21, 1970, by the District Court of the United States for the Eastern District of Pennsylvania, notice is hereby given that a hearing will be held on July 15, 1970, at 11:00 o'clock A.M., before that Court in Court Room No. 3, in the United States Court House, Ninth and Market Streets, in the City of Philadelphia, Pennsylvania, at which hearing or any adjournment thereof that Court will, pursuant to the provisions of Section 77 of the Bankruptcy Act (11 U.S.C. Sec. 205) relating to bankruptcy, appoint one or more trustees of the property of said Penn Central Transportation Company.

Dated, June , 1970.

IN THE
UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

—
No. 70 C 3205
—

GEORGE P. BAKER, RICHARD C. BOND, JERVIS
LANGDON, JR. AND WILLARD WIRTZ, TRUS-
TEES OF THE PROPERTY OF PENN CENTRAL
TRANSPORTATION COMPANY, DEBTOR,
Plaintiffs,

v.

GOLD SEAL LIQUORS, INC.,

Defendant.

—
MEMORANDUM OPINION AND ORDER.

This is an action by the trustees of the property of the Penn Central Transportation Company for unpaid freight charges for transportation performed by the Penn Central for and on behalf of defendant during the period August 22, 1968 to and including June 18, 1970. The defendant has filed a counterclaim alleging loss and damage to various shipments of merchandise handled by the Penn Central for defendant's account, and alleging that the freight charges as to these lost and damaged shipments have been paid.

The parties have filed a stipulation of facts in which they agree that \$6,999.76 in transportation charges is due and owing from defendant to plaintiffs and that \$18,016.77

is due and owing from plaintiffs to defendant for loss and damage to certain shipments.

The case is now before the Court on plaintiffs' motion for summary judgment in favor of each party for the stipulated amounts. Plaintiffs contend, however, that the law pertaining to the reorganization of a railroad does not permit a set-off of one judgment against the other, resulting in a net judgment for defendant. The question presented, then, is whether this Court should allow the set-off of one judgment against the other.

On June 21, 1970, the United States District Court for the Eastern District of Pennsylvania entered an order approving the petition of the Penn Central Transportation Company for reorganization under Section 77 of the Bankruptcy Act (11 U.S.C. § 205, et seq. Section 68(a) of the Bankruptcy Act (11 U.S.C. § 108(a)) provides that:

In all cases of mutual debts or mutual credits between the estate of a bankrupt and a creditor the account shall be stated and one debt shall be set off against the other, and the balance only shall be allowed or paid.

This case is collateral to the reorganization proceedings and was brought by the trustees in exercise of their power to gather assets and keep the business going. In such a suit, Section 68(a) applies only by way of analogy, based on the equities of the situation. *Lowden v. N. W. National Bank*, 298 U.S. 160 (1936).

The plaintiffs contend that Section 68(a), although unequivocal on its face, is generally not applied in reorganization cases as it is in straight bankruptcy proceedings since the purpose of reorganization is to "save a sick business, not to bury it and divide up its belongings." *Susquehanna Chemical Corp. v. Producers Bank & Trust Co.*, 174 F.2d 783, 787 (3rd Cir. 1949).

The plaintiffs have also pointed out that the reorganization court in which the Penn Central filed its petition for reorganization has consistently refused to allow set-offs. The set-offs involved there, however, were extra-judicial attempts at self-help which that court felt would hamper the administration of the reorganization.

The plaintiffs have cited no authority to support the entry of judgments on both the claim and counter-claim while at the same time denying a set-off of one against the other. Nor would that be the equitable course of action to follow in the instant case. The defendant is being precluded from satisfying *any* judgment it receives in the instant case as a result of the pending reorganization proceedings. It should not suffer further damage by being precluded from a set-off of its judgment against that of the plaintiffs.

For the reasons stated herein, the plaintiffs' motion for summary judgment is granted. The plaintiffs are indebted to the defendant in the amount of \$18,016.77 and the defendant is indebted to the plaintiffs in the amount of \$6,999.76. Therefore, a net judgment is hereby entered in favor of defendant and against plaintiffs in the amount of \$11,017.01.

ENTER:

ALEXANDER J. NAPOLI,
United States District Judge.

DATED: March 16th, 1972

COURT OF APPEALS OPINION.

(Filed August 23, 1973.)

IN THE
UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT

SEPTEMBER TERM, 1972—APRIL SESSION, 1973

No. 72-1386

GEORGE P. BAKER, RICHARD C. BOND,
JERVIS LANGDON, JR., AND WILLARD
WIRTZ, TRUSTEES OF THE PROPERTY
OF PENN CENTRAL TRANSPORTA-
TION COMPANY, DEBTOR,
Plaintiffs-Appellants,

v.

GOLD SEAL LIQUORS, INC.,
Defendant-Appellee.

Appeal from the
United States Dis-
trict Court for the
Northern District
of Illinois, Eastern
Division.

ALEXANDER, J.
NAPOLI, D.J.
No. 70 C 3205

ARGUED APRIL 20, 1973—DECIDED AUGUST 23, 1973

Before SWYGERT, *Chief Judge*, HASTINGS and MURRAH,*
Circuit Judges.

MURRAH, *Circuit Judge.* The trustees of the Penn
Central Transportation Company in a Section 77 reorgani-
zation proceeding in the District Court for the Eastern

* Alfred M. Murrah, of the Tenth Circuit, sitting by designation.

District of Pennsylvania brought this plenary suit in the Northern District of Illinois against Gold Seal Liquors, Inc. to recover \$6,999.76 for accrued freight charges. Gold Seal Liquors counterclaimed for \$18,016.77 for cargo loss and damages. The Illinois court allowed a setoff and rendered judgment against the trustees for the balance in the sum of \$11,017.01. The respective accounts are not disputed. The sole question is the propriety of the setoff.

It seems to be agreed that the setoff provisions of Section 68 of the Bankruptcy Act do not necessarily obtain in a reorganization proceeding of this kind. That is, see *Susquehanna Chemical Corp. v. Producers Bank & Tr. Co.*, 174 F.2d 783 (3d Cir. 1949), and *Lowden v. N. W. National Bank*, 298 U.S. 160 (1936). Nor do the trustees contend that the Illinois court was not empowered to grant the setoff. The contention is that "considerations of judicial comity should have persuaded" the Illinois court to honor Order No. 571 of the bankruptcy court enjoining all persons, firms and corporations holding credits for the account of the debtor from offsetting them against any obligation of the debtor.

Giving force and effect to Order No. 571, the bankruptcy court has held in a summary contempt proceeding that Section 77(a) conferred upon it "exclusive jurisdiction of the debtor and its property wherever located"; that choses in action are property of the debtor and in the actual or constructive possession of the debtor; and that it would prejudice the public interest in the continuation of railroad service to allow setoffs to deprive the debtor of sorely needed bank cash. See *Penn Cent. Tr. Co. v. National City Bank of Cleveland, Ohio*, 315 F. Supp. 1281 (E.D. Pa. 1970). The banks in that case were accordingly summarily ordered to restore the bank balances which they had set off against debts owed them by the railroad. 315 F. Supp. at 1285.

This order, however, did not undertake to formally adjudicate the rights of the parties, it merely restrained the banks from exercising the remedy of self-help. See 315 F. Supp. at 1284.

In a plenary suit indistinguishably similar to ours, the Indiana court declined to adjudicate the counterclaim or to allow a setoff on the grounds that, inasmuch as Order No. 571 expressly enjoined setoffs, counterclaims must be filed and adjudicated by the bankruptcy court along with the claims of other creditors. See *Penn Central Transp. Co. v. March Warehouse Corp.*, 356 F. Supp. 567 (S.D. Ind. 1972).

We cannot agree that "judicial comity" dictates forbearance of the exercise of the jurisdiction of the court in cases of this kind. The trustees having invoked the jurisdiction of the Illinois court for the adjudication of the railroad's claim, there is nothing in the principles of "judicial comity" to require the Illinois court to withhold the full exercise of its jurisdiction.

After all, plenary actions by trustees in a reorganization proceeding are nothing more than ordinary lawsuits. See, e.g., 5 Moore's Federal Practice ¶38.30(4). The power to adjudicate the subject matter is unquestioned and unquestionable. The Federal Rules of Civil Procedure undoubtedly apply (see 7 Moore's Federal Practice ¶81.04(1)), and a counterclaim is permissible, even compulsory (see Fed. R. Civ. P. 13(a)-(c), and 3 Moore's Federal Practice ¶¶ 13.12(1) and 13.13). Both the claim and the counterclaim are upon stated accounts—equitable principles do not serve to shape or fashion the relative rights and remedies of the parties.

The adjudication of the claims in the Illinois court is a matter of law. The satisfaction of the resulting judgment is subject to the equitable principles generally applicable in a court of bankruptcy. The judgment of the Illinois

court must now be submitted to the reorganization court with all other claims, to be satisfied in accordance with the appropriate orders of that court.

The judgment is affirmed.

Supreme Court of the United States

No. 73-804

George P. Baker, et al.,

Petitioners,

v.

Gold Seal Liquors, Inc.

ORDER ALLOWING CERTIORARI. Filed **January 21**, 19 **74**.

The petition herein for a writ of certiorari to the United States Court of Appeals for the **Seventh** Circuit is granted.

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FILED

NOV 20 1973

MICHAEL RODAK, JR., CL

Supreme Court of the United States

October Term, 1973.

No. 73 - 804

**GEORGE P. BAKER, RICHARD C. BOND, and JERVIS
LANGDON, JR., TRUSTEES OF THE PROPERTY OF
PENN CENTRAL TRANSPORTATION COMPANY,
Debtor,**

Petitioners,

v.

GOLD SEAL LIQUORS, INC.,

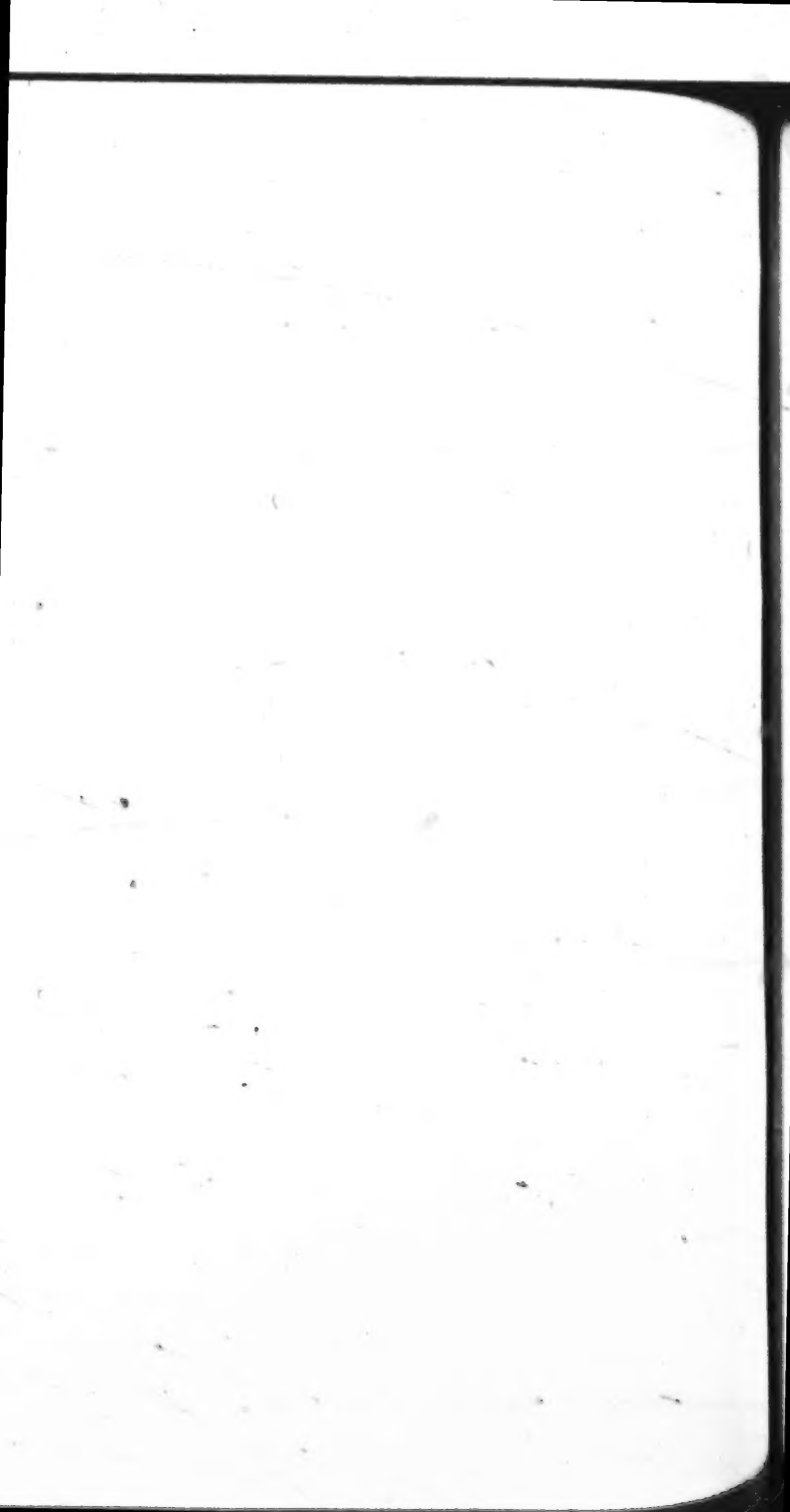
Respondent.

**PETITION FOR WRIT OF CERTIORARI TO THE
UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT**

**PAUL R. DUKE,
JOHN E. WALLACE, JR.,
1138 Six Penn Center Plaza,
Philadelphia, Pa. 19104**

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Chicago, Illinois. 60606**

Attorneys for Petitioners.



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IN THE

Supreme Court of the United States

OCTOBER TERM 1973.

No. _____.

GEORGE P. BAKER, RICHARD C. BOND, AND
JERVIS LANGDON, JR., TRUSTEES OF THE
PROPERTY OF PENN CENTRAL TRANSPORTA-
TION COMPANY, DEBTOR,

Petitioners,

v.

GOLD SEAL LIQUORS, INC.,

Respondent.

**PETITION FOR WRIT OF CERTIORARI TO THE
UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT.**

Petitioners George P. Baker, Richard C. Bond, and Jervis Langdon, Jr., Trustees of the Property of the Penn Central Transportation Company, Debtor in reorganization under Section 77 of the Bankruptcy Act (11 U.S.C. § 205), respectfully pray that a Writ of Certiorari issue to review the judgment and opinion of the United States Court of Appeals for the Seventh Circuit entered on August 23, 1973.

OPINIONS BELOW.

The findings of fact and opinion of the District Court for the Northern District of Illinois, entered February 18, 1972, are unreported and are printed in Appendix A hereto (A1-A3). The opinion of the panel of the Court of Appeals, entered on August 23, 1973, is not yet reported, and is printed in Appendix B (A4-A6).

JURISDICTION.

The judgment of the United States Court of Appeals for the Seventh Circuit was entered on August 23, 1973. This Court's jurisdiction is invoked under 28 U.S.C. § 1254(1).

QUESTION PRESENTED.

Did the court below err in holding that a shipper was entitled to a net judgment and consequently to effect a setoff where a railroad in reorganization sued the shipper for pre-reorganization freight charges and the shipper counterclaimed for pre-reorganization loss and damage to shipments and where the Reorganization Court had denied setoffs to other creditors in the reorganization proceedings.

STATEMENT OF THE CASE.

The facts in the case are quite simple. On June 21, 1970, Penn Central Transportation Company filed a Petition for Reorganization under Section 77 of the Bankruptcy Act (11 U.S.C. 205). The Petition was filed in the District Court for the Eastern District of Pennsylvania (Reorganization Court), under the caption "In the Matter of Penn Central Transportation Company, Debtor, No. 70-347," and on the same day the Reorganization Court entered Order No. 1 approving the Petition. Paragraph 10 of Order No. 1 provided:

"10. All persons, firms and corporations, holding collateral heretofore pledged by the Debtor as security for its notes or obligations or holding for the account of the Debtor deposit balances or credits be and each of them hereby are restrained and enjoined from selling, converting or otherwise disposing of such collateral, deposit balances or other credits, or any part thereof, or from off-setting the same, or any part thereof, against any obligation of the Debtor, until further order of this Court." (R. 32)¹

On July 22, 1970, pursuant to Court Order No. 20, George P. Baker, Richard C. Bond, Jervis Langdon, Jr., and Willard Wirtz were appointed Trustees of the Debtor. The Trustees, *inter alia*, sought to collect the assets of the Debtor's estate of which one was a claim for freight charges which Gold Seal Liquors owed to the Debtor.

On December 22, 1970, the Trustees brought suit in the United States District Court for the Northern District of Illinois against Gold Seal Liquors to recover \$8,256.61 in freight charges which had accrued during a period of approximately a year and a half prior to June 21, 1970 (R. 5-6).

1. The reference "R" is to the record in the Court of Appeals.

The cause of action arose under the laws of the United States regulating commerce, 49 U.S.C. §§ 3(2) and 6(7), and the District Court below had jurisdiction of the action under 28 U.S.C. § 1337. Gold Seal Liquors filed a counterclaim for \$19,319.42 for loss and damage to various shipments accruing over a period of approximately two years prior to June 21, 1970 (R. 11).

The parties filed a Stipulation of Facts in which Gold Seal Liquors admitted its liability to the Trustees in the amount of \$6,999.76, and the Trustees acknowledged their liability to Gold Seal Liquors in the amount of \$18,016.77 (R. 15-16).

Previous to the institution of this action, the Reorganization Court had prohibited various bank creditors from offsetting against the Debtor (*Penn Central Transportation Co. v. National City Bank of Cleveland, et al.*, 315 F. Supp. 1281 (E.D. Pa. 1970)) (Bank Setoff Case), and had under advisement a petition of the Trustees for an order directing certain shippers to pay amounts due Debtor and prohibiting the shippers from offsetting.

After the institution of this matter, but prior to a decision by the Illinois District Court, the Bank Setoff Case was affirmed by the Third Circuit Court of Appeals. *In re: Penn Central Transportation Co.*, 453 F.2d 520 (3d Cir. 1971), *cert. den.* 408 U.S. 923 (1972). Further, during the same period, the Reorganization Court entered Order No. 571 granting the Trustees' petition prohibiting certain shippers, *inter alia*, from setting off freight loss and damage claims against amounts owed the Debtor for freight transportation services. *In the Matter of Penn Central Transportation Company, Debtor*, 339 F. Supp. 603 (1972), *aff'd* 477 F.2d 841 (3d Cir. 1973), *cert. den.* — U.S. — (No. 72-1698, 42 U.S. Law Week 3213); *aff'd sub nom. U.S. Steel Corp. v. Trustees*, — U.S. — (No. 73-94, 42 U.S. Law Week

3213) (Shippers' Setoff Case). The Illinois District Court, nevertheless, permitted a setoff which resulted in a net judgment in favor of Gold Seal Liquors against the Trustees in the amount of \$11,017.01. The court held that, since an extra-judicial self-help setoff was not involved in the matter before it, setoff should be permitted.

An appeal was taken by the Trustees. The Circuit Court affirmed. Affirmance of the net judgment permitted Gold Seal Liquors to recover dollar for dollar on its pre-reorganization claim for loss and damage to the extent of the amount of the Trustees' admitted claim against Gold Seal, viz., \$6999.76.²

2. Although the Circuit Court stated that Gold Seal Liquors must now submit its claim on the judgment to the Reorganization Court (A6), it has, by affirming the net judgment, already permitted Gold Seal Liquors to recover \$6,999.76.

REASONS FOR GRANTING THE WRIT.

In sustaining the right of appellee to set off a pre-bankruptcy debt against the Debtor, the court below failed to give adequate consideration to the reasons for denying setoffs as the Reorganization Court had done. In so doing, the decisions below are in conflict with the result reached in the Third Circuit in the Bank Setoff Case and the Shippers' Setoff Case, and will afford shipper-claimants in the Seventh Circuit a preference as compared with all other shipper-claimants located elsewhere.

The decisions below are also in direct conflict with *Trustees of the Property of Penn Central Transportation Company, Debtor v. Southeastern Michigan Shippers Co-Operative Association*, (Civ. Action No. 39090 U.S. Dist. Ct. E.D. Mich.) (Memorandum Opinion printed in Appendix C hereto A7-A21.)

The decisions below, which give effect to Gold Seal Liquors, Inc. setoff, are in direct variance with Reorganization Court Order No. 1 enjoining setoffs, and have the effect of interfering with the Reorganization Court's exclusive jurisdiction over the property of the Debtor's estate, and the equitable treatment of claims against the estate. By affirming the entry of a net judgment in this matter, the Court of Appeals for the Seventh Circuit has disposed of property of the estate, i.e. an admittedly valid chose in action for \$6,999.76, by requiring it to be applied in partial payment of a pre-reorganization claim against the estate for loss or damage to freight. Section 77 of the Bankruptcy Act vests exclusive jurisdiction of such matters in the court supervising the reorganization of the debtor, here the U.S. District Court for the Eastern District of Pennsylvania. *In re New York, New Haven and Hartford Railroad Co.*, 457 F.2d 683 (2d Cir. 1972) cert. den. 409

U.S. 890 (1972); *Calloway v. Benton*, 336 U.S. 132, 147 (1949).

While the amount involved in this one proceeding is relatively small, there are several other suits pending in courts in the Seventh Circuit which would obviously be governed by this decision and, unless overturned, will result in claimants who happen to be sued in that Circuit receiving a clear preference over all other claimants with similar claims. This is grossly unfair, and should not be permitted to stand in light of the equitable considerations which caused the Reorganization Court to prohibit set-offs.

The Shipper Setoff Case (339 F. Supp. 603) arose out of a petition of the Trustees seeking an order directing numerous shippers to pay several million dollars in freight charges due the Debtor. These creditors had refused to pay the freight charges except to the extent a balance might be left after they had offset against the freight charges amounts which they claimed the Debtor owed them. The Reorganization Court first concluded that the Debtor had an obligation to collect freight charges due it, and the existence of claims against the Debtor did not change this. The Reorganization Court recognized that, but for reorganization, the shippers' claims against the Debtor could be litigated in actions brought by the Debtor to collect its freight charges. The question was whether the Court should exercise its discretion to enjoin setoffs.

The Reorganization Court reviewed the relevant factors and concluded that setoffs should not be permitted at this time. The relevant factors were as follows:

- 1) to permit the setoffs would be to discriminate against the vast majority of shippers who had paid their bankruptcy freight claims in full;

- 2) the cash need of the reorganization must be considered. It is more consistent with the overall purposes of Section 77 of the Bankruptcy Act that shipper claims be disposed of in the proofs of claim procedure rather than that current operating revenues of the Debtor should be jeopardized by setoffs; and
- 3) the Trustees, in the exercise of their business judgment, in an attempt to treat all parties fairly, requested that setoffs be restrained.

The Third Circuit Court of Appeals affirmed the summary jurisdiction of the Reorganization Court and reiterated that it was in that Court's sound discretion to determine "whether or not to permit setoff or counterclaim against the Debtor's charges." (477 F.2d at 845).

The Illinois District Court ignored the relevant factors set forth, and permitted Gold Seal Liquors the right of setoff by the entry of a net judgment in favor of Gold Seal. Petitioners agree that in the interest of judicial economy, the Illinois District Court could decide the counterclaim of Gold Seal Liquors. Indeed, considerations of practicality and judicial economy are what compelled the Trustees to liquidate their own claim in the District Court for the Northern District of Illinois. As is shown by the record herein, there was a dispute as to the actual amount owing to the Trustees on their chose in action for freight charges, and it was not until the factual dispute was resolved (here admittedly by way of stipulation) that the actual amount of the chose was liquidated. In a reorganization proceeding of this magnitude, to compel the Trustees to liquidate every chose in their possession in the Reorganization Court could bring the reorganization proceeding itself to a standstill.

The error committed by the Illinois District Court and affirmed by the court below was its refusal to enter separate judgments. By entering the net judgment it has effectively disposed of the Trustees' chose in action. The opinion of the court below gives lip service to the jurisdiction of the Reorganization Court by requiring that the resulting judgment "be submitted to the reorganization court with all other claims. . . ." (A6). However, by its affirmance of the net judgment, the court below has deprived the Reorganization Court of its jurisdiction over the valid chose in action which was the property of the Trustees.

Any recovery on the judgment entered on the counterclaim must be through the proof of claim procedure in the Reorganization Court. *Thompson v. Texas Mexican Ry. Co.*, 328 U.S. 134, 141 (1946). By failing to consider the reorganization proceedings of the Debtor, the courts below have discriminated in favor of Gold Seal Liquors to the detriment of other creditors of the Debtor. All other loss and damage claimants are relegated to the proof of claim procedure to recover any amounts owed to them. The judgment below has permitted Gold Seal Liquors to recover presently at least the amount of the setoff, \$6,999.76, 100 cents on the dollar.

A case similar to the instant one and involving Petitioner is *Trustees of the Property of Penn Central Transportation Company v. Southeastern Michigan Shippers Co-Operative Association* (A7-A21). Here also both parties were indebted to one another, and one of the issues was whether setoff should be permitted. The court analyzed the setoff issue thoroughly and concluded that ". . . this court is without power to effect a setoff of any amounts recovered." (A21). Nevertheless, in the interest of judicial economy, the Michigan District Court has permitted the

counterclaim to be prosecuted and, if succesful, has required that it be presented to the Reorganization Court for proof and allowance. This result correctly recognizes the exclusive jurisdiction of the Reorganization Court and highlights the error of the courts below here.

On the basis of the decision in the Shippers' Setoff Case, the courts below should have denied the right of setoff to Gold Seal Liquors. If the holding is permitted to stand, it will be controlling in the Seventh Circuit, and will have a detrimental effect upon the Debtor's estate. The Trustees will be faced with a Hobson's choice. They will have to forego the attempt to recover property of the estate in other forums, which is inconsistent with principles of judicial economy and efficiency. The alternative is to prosecute actions which will result in certain creditors' recovering all or part of their pre-bankruptcy claims, while other creditors are denied that right.

CONCLUSION.

We submit, therefore, that a Writ of Certiorari should be granted and that the decision below should be reversed.

Respectfully submitted,

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APPENDIX A.

DISTRICT COURT OPINION.

(Filed March 16, 1972.)

IN THE
UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

No. 70 C 3205

GEORGE P. BAKER, RICHARD C. BOND, JERVIS
LANGDON, JR. AND WILLARD WIRTZ, TRUS-
TEES OF THE PROPERTY OF PENN CENTRAL
TRANSPORTATION COMPANY, DEBTOR,

Plaintiffs,

v.

GOLD SEAL LIQUORS, INC.,

Defendant.

MEMORANDUM OPINION AND ORDER.

This is an action by the trustees of the property of the Penn Central Transportation Company for unpaid freight charges for transportation performed by the Penn Central for and on behalf of defendant during the period August 22, 1968 to and including June 18, 1970. The defendant has filed a counterclaim alleging loss and damage to various shipments of merchandise handled by the Penn Central for defendant's account, and alleging that the freight charges as to these lost and damaged shipments have been paid.

The parties have filed a stipulation of facts in which they agree that \$6,999.76 in transportation charges is due and owing from defendant to plaintiffs and that \$18,016.77

(A1)

is due and owing from plaintiffs to defendant for loss and damage to certain shipments.

The case is now before the Court on plaintiffs' motion for summary judgment in favor of each party for the stipulated amounts. Plaintiffs contend, however, that the law pertaining to the reorganization of a railroad does not permit a set-off of one judgment against the other, resulting in a net judgment for defendant. The question presented, then, is whether this Court should allow the set-off of one judgment against the other.

On June 21, 1970, the United States District Court for the Eastern District of Pennsylvania entered an order approving the petition of the Penn Central Transportation Company for reorganization under Section 77 of the Bankruptcy Act (11 U.S.C. § 205, et seq.). Section 68(a) of the Bankruptcy Act (11 U.S.C. § 108(a)) provides that:

In all cases of mutual debts or mutual credits between the estate of a bankrupt and a creditor the account shall be stated and one debt shall be set off against the other, and the balance only shall be allowed or paid.

This case is collateral to the reorganization proceedings and was brought by the trustees in exercise of their power to gather assets and keep the business going. In such a suit, Section 68(a) applies only by way of analogy, based on the equities of the situation. *Lowden v. N. W. National Bank*, 298 U.S. 160 (1936).

The plaintiffs contend that Section 68(a), although unequivocal on its face, is generally not applied in reorganization cases as it is in straight bankruptcy proceedings since the purpose of reorganization is to "save a sick business, not to bury it and divide up its belongings." *Susquehanna Chemical Corp. v. Producers Bank & Trust Co.*, 174 F.2d 783, 787 (3rd Cir. 1949).

The plaintiffs have also pointed out that the reorganization court in which the Penn Central filed its petition for reorganization has consistently refused to allow set-offs. The set-offs involved there, however, were extra-judicial attempts at self-help which that court felt would hamper the administration of the reorganization.

The plaintiffs have cited no authority to support the entry of judgments on both the claim and counter-claim while at the same time denying a set-off of one against the other. Nor would that be the equitable course of action to follow in the instant case. The defendant is being precluded from satisfying *any* judgment it receives in the instant case as a result of the pending reorganization proceedings. It should not suffer further damage by being precluded from a set-off of its judgment against that of the plaintiffs.

For the reasons stated herein, the plaintiffs' motion for summary judgment is granted. The plaintiffs are indebted to the defendant in the amount of \$18,016.77 and the defendant is indebted to the plaintiffs in the amount of \$6,999.76. Therefore, a net judgment is hereby entered in favor of defendant and against plaintiffs in the amount of \$11,017.01.

ENTER:

ALEXANDER J. NAPOLI,
United States District Judge.

DATED: March 16th, 1972

APPENDIX B.

COURT OF APPEALS OPINION.

(Filed August 23, 1973.)

IN THE
UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT

SEPTEMBER TERM, 1972—APRIL SESSION, 1973

No. 72-1386

GEORGE P. BAKER, RICHARD C. BOND,
JERVIS LANGDON, JR., AND WILLARD
WIRTZ, TRUSTEES OF THE PROPERTY
OF PENN CENTRAL TRANSPORTATION
COMPANY, DEBTOR,
Plaintiffs-Appellants,

v.

GOLD SEAL LIQUORS, INC.,
*Defendant-Appellee.*Appeal from the
United States Dis-
trict Court for the
Northern District
of Illinois, Eastern
Division.

ALEXANDER, J.

NAPOLI, D.J.

No. 70 C 3205

ARGUED APRIL 20, 1973—DECIDED AUGUST 23, 1973

Before SWYGERT, *Chief Judge*, HASTINGS and MURRAH,*
Circuit Judges.

MURRAH, *Circuit Judge.* The trustees of the Penn Central Transportation Company in a Section 77 reorganization proceeding in the District Court for the Eastern District of Pennsylvania brought this plenary suit in the Northern District of Illinois against Gold Seal Liquors, Inc. to recover \$6,999.76 for accrued freight charges. Gold Seal Liquors counterclaimed for \$18,016.77

* Alfred M. Murrah, of the Tenth Circuit, sitting by designation.

for cargo loss and damages. The Illinois court allowed a setoff and rendered judgment against the trustees for the balance in the sum of \$11,017.01. The respective accounts are not disputed. The sole question is the propriety of the setoff.

It seems to be agreed that the setoff provisions of Section 68 of the Bankruptcy Act do not necessarily obtain in a reorganization proceeding of this kind. That is, see *Susquehanna Chemical Corp. v. Producers Bank & Tr. Co.*, 174 F.2d 783 (3d Cir. 1949), and *Lowden v. N. W. National Bank*, 298 U.S. 160 (1936). Nor do the trustees contend that the Illinois court was not empowered to grant the setoff. The contention is that "considerations of judicial comity should have persuaded" the Illinois court to honor Order No. 571 of the bankruptcy court enjoining all persons, firms and corporations holding credits for the account of the debtor from offsetting them against any obligation of the debtor.

Giving force and effect to Order No. 571, the bankruptcy court has held in a summary contempt proceeding that Section 77(a) conferred upon it "exclusive jurisdiction of the debtor and its property wherever located"; that choses in action are property of the debtor and in the actual or constructive possession of the debtor; and that it would prejudice the public interest in the continuation of railroad service to allow setoffs to deprive the debtor of sorely needed bank cash. See *Penn Cent. Tr. Co. v. National City Bank of Cleveland, Ohio*, 315 F. Supp. 1281 (E.D. Pa. 1970). The banks in that case were accordingly summarily ordered to restore the bank balances which they had set off against debts owed them by the railroad. 315 F. Supp. at 1285. This order, however, did not undertake to formally adjudicate the rights of the parties, it merely restrained the banks from exercising the remedy of self-help. See 315 F. Supp. at 1284.

In a plenary suit indistinguishably similar to ours, the Indiana court declined to adjudicate the counterclaim or to allow a setoff on the grounds that, inasmuch as Order No. 571 expressly enjoined setoffs, counterclaims must be filed and adjudicated by the bankruptcy court along with the claims of other creditors. *See Penn Central Transp. Co. v. March Warehouse Corp.*, 356 F. Supp. 567 (S.D. Ind. 1972).

We cannot agree that "judicial comity" dictates forbearance of the exercise of the jurisdiction of the court in cases of this kind. The trustees having invoked the jurisdiction of the Illinois court for the adjudication of the railroad's claim, there is nothing in the principles of "judicial comity" to require the Illinois court to withhold the full exercise of its jurisdiction.

After all, plenary actions by trustees in a reorganization proceeding are nothing more than ordinary lawsuits. *See, e.g.*, 5 Moore's Federal Practice ¶ 38.30(4). The power to adjudicate the subject matter is unquestioned and unquestionable. The Federal Rules of Civil Procedure undoubtedly apply (*see* 7 Moore's Federal Practice ¶ 81.04 (1)), and a counterclaim is permissible, even compulsory (*see* Fed. R. Civ. P. 13(a)-(c), and 3 Moore's Federal Practice ¶¶ 13.12(1) and 13.13). Both the claim and the counterclaim are upon stated accounts—equitable principles do not serve to shape or fashion the relative rights and remedies of the parties.

The adjudication of the claims in the Illinois court is a matter of law. The satisfaction of the resulting judgment is subject to the equitable principles generally applicable in a court of bankruptcy. The judgment of the Illinois court must now be submitted to the reorganization court with all other claims, to be satisfied in accordance with the appropriate orders of that court.

The judgment is affirmed.

APPENDIX C.

CONFLICTING OPINION.

(Filed September 28, 1973.)

**UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF MICHIGAN
SOUTHERN DIVISION.**

Civil Action

No. 39090.

**GEORGE P. BAKER, RICHARD C. BOND, JERVIS
LANGDON, JR., AND WILLARD WIRTZ, TRUSTEES
OF THE PROPERTY OF PENN CENTRAL TRANS-
PORTATION COMPANY, A PENNSYLVANIA CORPORA-
TION, DEBTOR,**

Plaintiffs,

v.

**SOUTHEASTERN MICHIGAN SHIPPERS CO-OP-
ERATIVE ASSOCIATION, A/K/A SEMCO, INC., A
MICHIGAN CORPORATION,**

Defendant.

MEMORANDUM OPINION.

Plaintiffs (trustees of the property of Penn Central Transportation Company) sue for freight charges totaling \$22,773.19 incurred by defendant (SEMCO, Inc.) between October 10, 1969, and November 11, 1969. Defendant pleads a prior accord and satisfaction and, in the alternative, counterclaims against plaintiffs in the amount of \$20,179.80 for damages to cargo sustained on February 21, 1969, and

March 3, 1969. It is these damage claims which defendant contends were previously set off against the freight charges now sought by plaintiffs, the difference of \$1,852.07 having been tendered and accepted on November 17, 1969.

Accord and Satisfaction.

It appears that SEMCO did try to arrange a mutual cancellation of accounts—the railroad's carriage charges against the shipper's claims for damages to cargo. Based on the facts elicited on these cross-motions for summary judgment, however, it is unclear whether these efforts came to a legally effective fruition.¹ There are genuine and material issues of fact yet to be decided on this question, and if there were no other factors involved, this case would be inappropriate for summary disposition. This result is complicated and somewhat altered by two additional facts: (1) the freight charges involved here are covered by the Interstate Commerce Act² and (2) since these claims accrued

1. "We recognize the Michigan rule that to constitute an accord and satisfaction, the tender of payment as being in full should be made in unequivocal terms so that the creditor in accepting the payment will do so understandingly. *Durkin v. Everhot Heater Co.*, 266 Mich. 508, 513, 254 N.W. 187 [1934]." *Allstate Ins. Co. v. Springer*, 269 F.2d 805, 809 (6th Cir. 1959), cert. denied, 361 U.S. 932 (1960). See also *Lafferty v. Cole*, 339 Mich. 223, 228 (1954) (creditor must be "fully informed of the condition accompanying acceptance"). This is merely a corollary to the general principle that an accord requires a meeting of the minds of the parties in an agreement to substitute one type of performance for another. See *Stadler v. Ciprian*, 265 Mich. 252, 262 (1933).

Here the evidence indicates that defendant's offer of settlement was ambiguous and equivocal. In a letter dated November 19, 1969, defendant's executive manager indicated that the off-setting of accounts and payment of the difference did not mean that SEMCO was declining payment of the freight charges, but that they would be paid as soon as the damage claims were approved by the railroad. Without further proof of the parties' intentions, this is insufficient to prove the existence (or nonexistence) of the claimed accord.

2. 49 U.S.C. § 1 *et seq.*

the railroad has entered into reorganization under the Bankruptcy Act.³

First, plaintiffs argue that whether or not the facts make out an accord and satisfaction is in the end irrelevant, for Section 6(7) of the Interstate Commerce Act⁴ absolutely prohibits and nullifies such arrangements. That section, prompted by a congressional purpose to eliminate secret preferences and kickbacks to shippers,⁵ mandates strict adherence to published tariffs.⁶ In applying this provision, the Supreme Court has held that a carrier may be compensated for its services only by payment in cash⁷

3. Reorganization of the Penn Central Transportation Company under 11 U.S.C. § 205 was initiated by an order of the District Court for the Eastern District of Pennsylvania on June 21, 1970 [hereinafter cited as Order No. 1], approving the railroad's petition and containing various provisions concerning its continued operation. Relevant materials may be found in the Corporate Reorganization Reporter (Penn Central).

4. "No carrier, unless otherwise provided by this chapter, shall engage or participate in the transportation of passengers or property, as defined in this chapter, unless the rates, fares, and charges which the same are transported by said carrier have been filed and published in accordance with the provisions of this chapter; nor shall any carrier charge or demand or collect or receive a greater or less or different compensation for such transportation of passengers or property, or for any service in connection therewith, between the points named in such tariffs than the rates, fares, and charges which are specified in the tariff filed and in effect at the time; nor shall any carrier refund or remit in any manner or by any device any portion of the rates, fares, and charges so specified, nor extend to any shipper or person any privileges or facilities in the transportation of passengers or property, except such as are specified in such tariffs." 49 U.S.C. § 6(7).

5. See, e.g., *Atchison, T. & S.F. Ry. Co. v. Bouziden*, 307 F.2d 230, 234 (10th Cir. 1962); *Baker v. Prolerized Chicago Corp.*, 335 F. Supp. 183, 185 (N.D. Ill. 1971). See also 49 U.S.C. § 3(1) (prohibiting preferences or prejudices).

6. "The lawful rate is that which the carrier *must* exact and that which the shipper *must* pay." *Kansas City So. Ry. Co. v. Carl*, 227 U.S. 639, 653 (1913) (emphasis added).

7. *Louisville & N.R. Co. v. Mottley*, 219 U.S. 467, 477 (1911).

or by check⁸ or by way of judicial set-off against judgments due the shipper.⁹ Any form of payment containing the potential for departure from the exact letter of the tariffs (such as the supplying of goods and services in exchange for carriage)¹⁰ is prohibited.

Defendant argues that the exception for judicial set-offs, enunciated by the Court in *Chicago & N.W. Ry. Co. v. Lindell*, 281 U.S. 14 (1930), should be extended to a prior set-off of accounts (rather than judgments) concluded informally between the parties. Defendant cites no cases supporting this position. *Burlington Northern Inc. v. United States*, 462 F.2d 526 (Ct. Cl. 1972), falls squarely within the *Lindell* exception. "According to plaintiff's reading, there can be no deduction of a damage claim against transportation charges except by adjudication of a court. But that is exactly the situation we have here." 462 F.2d at 529. The same is true of *Yale Express System, Inc. v. Nogg*, 362 F.2d 111 (2nd Cir. 1966), and *Southern Pacific Co. v. Miller Abattoir Co.*, 454 F.2d 357 (3rd Cir. 1972).

On the other hand, at least two courts have squarely faced the issue of whether non-judicial set-offs are permissible under the Interstate Commerce Act, and have determined that they are not.

"Another group of shippers contend that, prior to bankruptcy, there was an agreed settlement of mutual accounts between the Debtor and the shipper, with the result that the Debtor either owes money to the shippers, or is owed much less than is now being claimed by the Trustees. . . . To the extent that the Debtor's claims against these companies were based on freight

8. *Fullerton Lumber Co. v. Chicago, M., St. P. & P.R. Co.*, 282 U.S. 520, 522 (1931).

9. *Chicago & N.W. Ry. Co. v. Lindell*, 281 U.S. 14, 17 (1930).

10. *Chicago, I. & L. Ry. Co. v. United States*, 219 U.S. 486, 496-97 (1911).

charges, it is clear under the principles set forth previously that they were incapable of being discharged either by unilateral set-offs or by mutual agreement." *In re Penn Central Transportation Co.*, 339 F. Supp. 603, 607 (E.D. Pa. 1972).

This conclusion was specifically approved by the Third Circuit:

"[One of the appellants] contends that under applicable Pennsylvania law, it extinguished its debt to the railroad by the nonjudicial set-off of a debt owed to it by the carrier Even assuming the validity of appellant's contention under Pennsylvania law, such a set-off would have been in express contravention of the Interstate Commerce Act. Indeed, the Act was so designed to prevent the kind of secret kickbacks which this type of practice could lead to." *In re Penn Central Transportation Co.*, 477 F.2d 841, 845 (3rd Cir. 1973).

The reason for distinguishing between judicial and non-judicial set-offs is obvious. In the former case, there is no adjustment until the exact value of each party's claim has been authoritatively determined; in the latter instance, there is no guarantee that the debt off-set against the freight charges is worth the amount allowed. When the set-off is judicially supervised, there is little opportunity for collusion; when it is privately arranged, there is no such assurance. In short, it is the policy of the Act to permit payment of freight charges only in a manner offering little or no opportunity for evasion of the tariff. Judicial set-offs satisfy this requirement while private arrangements do not.

As a result, the accord and satisfaction pleaded by defendant, even if convincingly established, is inadequate to resist the trustees' cause of action. Because defendant

interposes no other defenses,¹¹ plaintiffs are entitled to summary judgment for the undisputed portion of their claim—\$22,039.89—minus the \$1,852.07 previously paid. There is a genuine dispute of fact as to waybills 223588 and 228460, totaling \$733.32, which must be resolved at trial.

The Counterclaim.

The railroad's reorganization raises a second question, namely whether the defendant may nevertheless recover in this court on its counterclaim. Initially, it should be noted that its claim is contested, both as to liability and damages. There has been presented no evidence from which this court can decide the issues raised, and therefore the defendant's cross-motion for summary judgment must be denied in any event.

Under *Lindell*, this court would ordinarily be authorized to proceed to judgment on the counterclaim and off-set any recovery thereunder against plaintiff's recovery. The problem is to determine what effect the intervening reorganization may have on the defendant's cause of action. Two issues must be considered: (1) whether the action may be maintained in this court and (2) if so, whether this court is empowered to set off any recovery against that of plaintiff (i.e., in effect to execute upon the judgment).

1. *Set-off.* Taking the second point first, this court is immediately confronted with 11 U.S.C. § 205(a), which gives the bankruptcy court in a railroad reorganization "exclusive jurisdiction of the debtor and its property wherever located" "Property" in the bankruptcy setting includes a cause of action such as that asserted by

11. "The Consignee alleged the Railroad's breach both as a defense and as a counterclaim. The alleged breach, however, does not constitute a defense to the Railroad's claim for freight charges, but constitutes an independent claim. . . ." *Southern Pacific Co. v. Miller Abattoir Co.*, 454 F.2d 357, 362 (3rd Cir. 1972).

the trustees in this case¹² and any recovery granted thereunder.¹³ "Exclusive jurisdiction" is generally given a literal interpretation.¹⁴ It follows that this court can exercise jurisdiction over the bankrupt's property, including a judgment or cause of action, only to the extent permitted by the bankruptcy court.¹⁵

That court, by its order of June 21, 1970, has authorized the trustees to institute and prosecute in any court suits for the recovery or protection of its property or rights,¹⁶ and to settle or defend claims against the debtor,¹⁷ including, in their discretion, "claims for loss, damage or delay to freight and baggage" ¹⁸

"[B]ut no payment shall, without further order of this Court, be made by the Debtor in respect of any such actions, proceedings or suits on claims accruing prior to the date of this order except such claims as may be permitted to be paid by this order or by other general orders hereafter entered herein, and such as constitute preferred claims under the Acts of Congress relating to bankruptcy; and no action taken by the Debtor in defense or settlement of such claims, actions, proceedings, or suits shall have the effect of establishing any claim upon, or right in, the property or funds in the possession of the Debtor that otherwise would not exist." ¹⁹

12. 11 U.S.C. § 110(a)(6).

13. *Meyer v. Fleming*, 327 U.S. 161, 165 (1946).

14. See, e.g., *In re New York, N.H. & H.R. Co.*, 457 F.2d 683, 689 (2nd Cir. 1972); *In re Imperial "400" National, Inc.*, 429 F.2d 671, 676-77 (3rd Cir. 1970).

15. *Cf. Warren v. Palmer*, 310 U.S. 132 (1940); *Ex parte Baldwin*, 291 U.S. 610 (1934).

16. Order No. 1, *supra*, note 3, ¶ 5.

17. *Id.*

18. *Id.*, ¶ 3B.

19. *Id.*, ¶ 5.

Thus, it appears that this court is empowered to adjudicate the plaintiffs' claim, but that it has no authority to dispose of any recovery upon that claim, whether by way of set-off or otherwise. Even if this court may also hear defendant's counterclaim (a matter yet to be decided), it may not satisfy that judgment out of the debtor's property, including its judgment in this suit. Once "the claim is reduced to judgment [it] may then be presented to the bankruptcy court for proof and allowance." *Thompson v. Texas Mexican Ry. Co.*, 328 U.S. 134, 141 (1946).

2. *Authority to Entertain Counterclaim.* The bankruptcy court has exclusive jurisdiction over not only the debtor's property, but over "any rights that may be asserted against it. These rights may be altered in any way thought necessary to achieve sound financial and operating conditions for the reorganized company, subject to the requirements of the Act." *Callaway v. Benton*, 336 U.S. 132, 147 (1949). In a railroad reorganization the class of claims included within the scope of this power is very great. "The term 'claims' includes debts, whether liquidated or unliquidated, securities (other than stock and option warrants to subscribe to stock), liens, or other interests of whatever character." 11 U.S.C. § 205(b).²⁰

In essence, the bankruptcy court may modify in any way it feels necessary any right asserted against the debtor which might adversely affect the reorganization plan. The fact that it is raised in the form of a counterclaim to a suit instituted by the trustees is irrelevant. The counterclaim is not a defense to the original claim, but an independent claim which must be approached on its own merits.²¹

20. Also cf. 11 U.S.C. § 205(b): "The term 'creditors' shall include, for all purposes of this section all holders of claims of whatever character against the debtor or its property, whether or not such claims would otherwise constitute provable claims under this Act."

21. See note 11, *supra*.

11 U.S.C. § 108, authorizing certain set-offs and counterclaims in ordinary bankruptcy, is not binding in Chapter X corporate reorganization cases, where it could defeat the very purpose of the reorganization by depriving the debtor corporation of much-needed working capital, thus endangering its ability to continue in operation.²² In railroad reorganizations, where the public interest in survival of the enterprise is even more compelling, the reorganization court may not only enjoin set-offs,²³ but may go further and

" . . . enjoin or stay the commencement or continuation of suits against the debtor until after final decree; and may, upon notice and for cause shown, enjoin or stay the commencement or continuance of any judicial proceeding to enforce any lien upon the estate until after final decree: *Provided*, That suits or claims for damage caused by the operation of trains, busses, or other means of transportation may be filed and prosecuted to judgment in any court of competent jurisdiction and any order staying the prosecution of any such cause of action or appeal shall be vacated." 11 U.S.C. § 205(j).

The Penn Central reorganization court has enjoined certain set-offs,²⁴ which the parties seem to have assumed

22. *Lowden v. Northwestern National Bank*, 298 U.S. 160, 163-66 (1936); *In re Yale Express System*, 362 F.2d 111, 116-17 (2d Cir. 1966); *Susquehanna Chemical Corp. v. Producers Bank & Trust Co.*, 174 F.2d 783, 787 (3rd Cir. 1949).

23. *Penn Central Transportation Co. v. National City Bank of Cleveland*, 315 F. Supp. 1281, 1283-84 (E.D. Pa. 1970), affirmed sub nom *In re Penn Central Transportation Co.*, 453 F.2d 520, 522-23 (3rd Cir. 1972).

24. "All persons, firms and corporations, holding collateral heretofore pledged by the Debtor as security for its notes or obligations or holding for the account of the Debtor deposit balances or credits be and each of them hereby are restrained and enjoined

are applicable in this case, though the assumption is a rather questionable one. This point is mooted, however, by the court's broader command that:

"All persons and all firms and corporations, whatsoever and wheresoever situated, located or domiciled, hereby are restrained and enjoined from interfering with, seizing, converting, appropriating, attaching, garnisheeing, levying upon, or enforcing liens upon, or in any manner whatsoever disturbing any portion or the assets, goods, money, deposit balances, credits, choses in action, interests, railroads, properties or premises belonging to, or in the possession of the Debtor as owner, lessee or otherwise, or from taking possession of or from entering upon, or in any way interfering with the same, or any part thereof, or from interfering in any manner with the operation of said railroads, properties or premises or the carrying on of its business by the Debtor under the order of this Court and from commencing or continuing any proceeding against the Debtor, whether for obtaining or for the enforcement of any judgment or decree or for any other purpose, provided that suits or claims for damages caused by the operation of trains, buses, or other means of transportation may be filed and prosecuted to judgment in any Court of competent jurisdiction"

Because of the bankruptcy court's exclusive jurisdiction over such matters, that mandate is binding upon this court.

24. (Cont'd.)

from selling, converting or otherwise disposing of such collateral, deposit balances or other credits, or any part thereof, or from offsetting the same, or any thereof, [sic] against any obligation of the Debtor, until further order of this Court." Order No. 1, *supra* note 3, ¶ 10 (footnote omitted).

25. *Id.*, ¶ 9.

Thus the ultimate issue is whether the proviso in subsection (j) of the statute, incorporated verbatim in the court's order, applies to defendant's counterclaim. If it constitutes a claim "for damages caused by the operation of trains, busses, or other means of transportation," it is cognizable in this court. If not, it falls within the scope of the order and its prosecution here is effectively enjoined.

There is relatively little case law interpreting the proviso, and what there is is either contradictory or inconclusive. Certainly "[t]he language of the proviso in § 77(j) is sufficiently broad to include all tort or contract claims whatsoever that arise from the operation of the trains or busses of the debtor." 5 *Collier on Bankruptcy* ¶ 77.12 at 516 (14th ed. 1970). Such a literal reading of the statute would clearly place SEMCO's counterclaim within the proviso. On their facts, several cases from the New York courts appear to support this result. See *Erie R. Co. v. William J. Pfeil, Inc.*, 11 N.Y.S.2d 155, 256 App. Div. 465 (1939) (counterclaim for damage to shipment of beans caused by salt in car held to be within proviso; counterclaim for breach of contract to construct a side track was outside proviso); *Yerckes-Eichenbaum, Inc. v. McCarthy*, 35 N.Y.S.2d 527, 264 App. Div. 403 (1942) (action for breach of contract of carriage within proviso); *Liquid Carbonic Corporation v. Erie R. Co.*, 14 N.Y.S.2d 168, 171 Misc. 969 (1939) (damage to cargo caused by failure to provide proper unloading facilities held to be within proviso). On the other hand, an opinion of the Seventh Circuit Court of Appeals of about the same vintage discusses the proviso at length, and concludes that Congress intended only to exempt personal injury claims. *In re Chicago & E. I. Ry. Co.*, 121 F.2d 785, 789 (7th Cir. 1941), cert. denied sub nom. *Chicago & E. I. Ry. Co. v. Gourley*, 314 U.S. 653 (1941). Two other federal courts have effectively avoided the issue in personal injury cases, which are uniformly recognized as

falling within the proviso. *Munnelly v. Farrell*, 317 F. Supp. 329 (S.D.N.Y. 1970); *Rodabaugh v. Denny*, 24 F. Supp. 1011 (S.D.N.Y. 1938). Finally, one other federal court seemed in passing to endorse the personal injury restriction, but went on to hold that a penalty for violation of the Safety Appliance Act is outside the proviso without ever defining its exact scope. *United States v. Dorigan*, 236 F. Supp. 106, 108 (E.D.N.Y. 1964).

It seems a sound rule of construction to adopt the simplest, most obvious interpretation of statutory language, unless there are clearly shown, persuasive reasons for doing otherwise.²⁶ A court may reasonably adopt a narrower or broader construction when to do so would better effectuate legislative intent.²⁷ This imperfectly expressed intent may have been actual (often discovered in legislative history) or it may be implied (a euphemism for the judicial rounding off of a law's sharp corners). But however the burden of justifying a non-literal interpretation is formulated, it has not been satisfied here. There is no legislative history to indicate that Congress intended something other than what it appeared to say. There is no evidence of overriding policies or dysfunctional effects which would permit this court to conclude that Congress should or would have in-

26. "True, courts in the interpretation of a statute have some scope for adopting a restricted rather than a liberal or a usual meaning of its words where acceptance of that meaning would lead to absurd results, . . . or would thwart the obvious purpose of the statute. . . . But courts are not free to reject that meaning where no such consequences follow and where, as here, it appears to be consonant with the purposes of the Act as declared by Congress and plainly disclosed by its structure." *Helvring v. Hammel*, 311 U.S. 504, 510-11 (1941).

27. "It is well established, however, that a meaning not conveyed by the literal language may be given in order to carry out the legislative intention, if the words used will bear such meaning." *United States v. Breenan*, 214 F.2d 268, 270 (D.C. Cir. 1954), cert. denied, 348 U.S. 830 (1954).

tended something else, and to impute to it such intent *nunc pro tunc*.

Indeed, to the extent there are such factors, they weigh in favor of a literal reading of the proviso. First, it would not alter the bankruptcy court's power to rule on the allowance of such claims, thus producing no interference with any part of the reorganization plan (which is the primary *raison d'être* for this section of the statute).

Second, the policy behind the subsection (j) proviso itself appears to be similar to that behind 28 U.S.C. § 959, permitting suit without leave of the bankruptcy court respecting acts or transactions of the trustees in "carrying on" the debtor's business. Referring to a predecessor of that section, the Supreme Court observed that:

"This act abrogated the rule that a receiver could not be sued without leave of the court appointing him, and gave the citizen the unconditional right to bring his action in the local courts, and to have the justice and amount of his demand determined by the verdict of a jury. He ceased to be compelled to litigate at a distance, or in any other forum, or according to any other course of justice, than he would be entitled to if the property or business were not being administered by the Federal court.

"The object of the section is manifest, and it is equally plain that that object would be open to be defeated if the receiver could remove the case at his volition. The intention to permit this to be done cannot reasonably be imputed to Congress, and, moreover, such a right would be inconsistent with the general policy of the act." *Gableman v. Peoria, D. & E. Ry. Co.*, 179 U.S. 335, 338 (1900).

Such a rationale suggests no basis for distinguishing between claims for property damage and those for personal

injury. Judge Patterson, in the *Rodabaugh* case, reached a similar conclusion in an analogous situation:

"In a very broad sense every action against a railroad company wherein money damages are demanded is an action for 'damages caused by the operation of trains, busses, or other means of transportation.' The primary business of a railroad company is to operate trains, and all its activities are incidental to the operation of trains. The words of the proviso are not to be construed so broadly; nor on the other hand, should they be construed so narrowly as to defeat the purpose of Congress in enacting the proviso. Congress doubtless had in mind the fact that the district court in charge of reorganization might be a long distance from the court in which an action for damages might be brought, and that the obtaining of consent of the court in charge of reorganization might be a hardship on a claimant. This is a factor in favor of a liberal interpretation of the proviso. There is no apparent reason for a distinction between the case of a plaintiff who is struck by a moving train and the case of a plaintiff who was injured by the collapse of a scaffold while working as an employee of the railroad. I am of opinion [sic] that the present case is one 'for damages caused by the operation of trains, busses or other means of transportation' and that the prosecution of the action in the usual manner has not been restrained by the reorganization court." 24 F. Supp. at 1012.

Finally, it must be remembered that defendant presses its claim in this court only in response to one initiated here by the trustees themselves. To hear the plaintiffs' case but not the defendant's, when both might easily be disposed of in one action, seems not only an uneconomic allocation of judicial resources but also an unduly harsh and useless

result. As a general rule, statutes should be construed so as to avoid the imposition of such arbitrary and meaningless hardships.²⁸

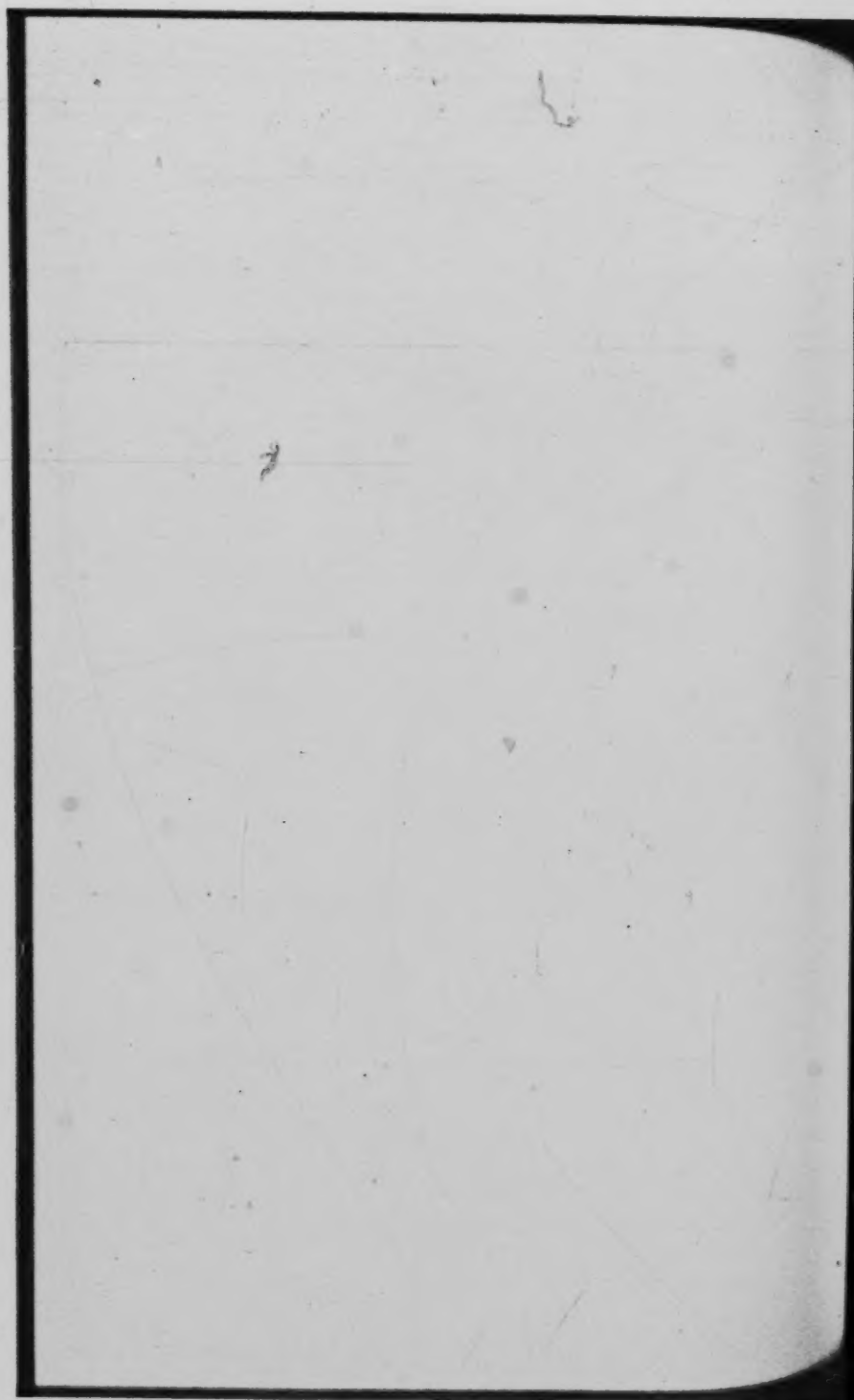
For these reasons, summary judgment will enter in favor of plaintiffs for the undisputed portion of their claim. The remainder of their claim, as well as defendant's counterclaim, may be prosecuted in this court. However, this court is without power to effect a set-off of any amounts recovered pursuant thereto.

An appropriate order may be submitted.

JOHN FEIKENS,
United States District Judge.

DATED: DETROIT, MICHIGAN
SEPTEMBER 28, 1973.

28. "The courts draw back from the construction of an ambiguous statute that would lead to unjust results, just as nature draws back from the consistency of one of its laws that would encase in ice fish at the bottom of a river." *Voris v. Gulf-Tide Stevedores*, 211 F.2d 549, 552-53 (5th Cir. 1954), cert. denied, 348 U.S. 823 (1954).



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MICHAEL ROBAK, JR.

No. 73-804

**In the
Supreme Court of the United States**

OCTOBER TERM, 1973

**GEORGE P. BAKER, RICHARD C. BOND, and
JERVIS LANGDON, JR., TRUSTEES OF THE PROP-
ERTY OF PENN. CENTRAL TRANSPORTATION
COMPANY, Debtor,**

Petitioners,

vs.

GOLD SEAL LIQUORS, INC.,

Respondent.

**BRIEF OF RESPONDENT IN OPPOSITION TO
PETITION FOR WRIT OF CERTIORARI TO THE
UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT**

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IN THE
SUPREME COURT OF THE UNITED STATES
OCTOBER TERM, 1973

No. 73-804

GEORGE P. BAKER, RICHARD C. BOND, and
JERVIS LANGDON, JR., TRUSTEES OF THE PROP-
ERTY OF PENN CENTRAL TRANSPORTATION
COMPANY, Debtor,

Petitioners,

vs.

GOLD SEAL LIQUORS, INC.,

Respondent.

**BRIEF OF RESPONDENT IN OPPOSITION TO
PETITION FOR WRIT OF CERTIORARI TO THE
UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT**

OPINIONS BELOW

The findings of fact and opinion of the District Court for the Northern District of Illinois, entered February 18, 1972, are unreported and appear as Appendix A to the Petition. The opinion of the Court of Appeals for the Seventh Circuit is reported at 484 F. 2d 950 (7th Cir. 1973).

JURISDICTION

The jurisdictional requisites are adequately set forth in the Petition.

QUESTION PRESENTED

Was the Court below correct in holding that the District Court below was not bound by Order No. 571, entered by the District Court for the Eastern District of Pennsylvania in the Penn-Central Reorganization proceedings?

STATEMENT OF THE CASE

Petitioners commenced a plenary action on December 22, 1970 in the United States District Court for the Northern District of Illinois, Eastern Division, to recover unpaid freight charges. Respondent counterclaimed for losses incurred from damage to shipments of merchandise bought by Respondent but delivered by Penn Central. Respondent's damages were almost three times the amount claimed by Petitioners.

The District Court, on the basis of stipulated facts, found Petitioners indebted to the Respondent for \$18,016.77, the Respondent indebted to Petitioners for \$6,999.76, and entered judgment in favor of Respondent for \$11,017.01.

Petitioners appealed to the Court of Appeals for the Seventh Circuit which affirmed the District Court, holding that Order No. 571 of the Reorganization Court, reported in 339 Fed. Supp. 603 did not oblige the Illinois Court to withhold the full exercise of its jurisdiction in Petitioners' plenary suit in that forum.

ARGUMENT

There is no conflict between the Circuits.

The opinion of the District Court of the Eastern District of Michigan, in *George P. Baker, et al. Trustees of the Property of Penn Central Transportation Company, a Pennsylvania Corporation, Debtor, Plaintiffs, v. Southeastern Michigan Shippers Co-Operative Association, a Michigan Corporation, Defendant*, printed as Appendix C to the Petition, is not an expression of the law of the highest court of the Circuit.

Southeastern Michigan Shippers was decided on cross-motions for summary judgment. The Court denied the defendant's motion for summary judgment on its counterclaim on evidentiary grounds. The counterclaim being contested, and no evidence being offered to enable the Court to decide issues of the motion, summary judgment on the counterclaim was properly denied.

It should be noted that the Michigan court recognized the distinction between judicial and non-judicial setoffs which was an important factor in distinguishing the various reorganization decisions cited by Petitioners here and below from the law applicable to this case.

The Michigan court observed that there was little case law on the subject. We suggest that until the Seventh Circuit spoke in the case now before this Court, there was almost none. Apparently, the Michigan court in *Southeastern Michigan Shippers* had not seen the decision of the Seventh Circuit, since it was not cited or noted, and in fact did not appear in the advance sheets of the Federal Reporter, Second Series until issue No. 3 of 484 F. 2d, dated November 19, 1973. Perhaps it might have

considered further the extent of its jurisdiction with a different result.

The reasoning of the panel of the Seventh Circuit, it is submitted, leads to a more and just result than that contended for by Petitioners.

In re New York, New Haven and Hartford Railroad Company, 457 F.2d 683 (2d Cir. 1972) dealt with the question of which reorganization court, the Connecticut court, administering the New Haven reorganization, or the Pennsylvania court administering the Penn Central reorganization, had jurisdiction over property of the Penn Central acquired from the New Haven. There was no question of counterclaim or setoff, between creditor, debtor and the railroad, as in the case here on Petition but rather a conflict between two federal district courts sitting as reorganization courts, each claiming subject-matter jurisdiction over the same property at the same time. The jurisdiction of the Pennsylvania court was upheld, and the Connecticut court was declared to be without subject-matter jurisdiction, 457 F.2d at P. 691. Such is not the situation in the instant case where the Illinois court had subject-matter jurisdiction of the plenary suit instituted by Petitioners.

Calloway v. Benton, 336 U.S. 132 (1949) affords Petitioners little help. There this Court affirmed a decision of the Court of Appeals which reversed the action of a reorganization court in enjoining state court proceedings involving matters of state law affecting a lessor of property leased by a railroad in reorganization.

Order No. 571, of the Reorganization Court, cited by Petitioners as the "Shipper Setoff Case," is not applicable here. The Court of Appeals noted in its review, at 477 F.2d 843:

"The basic issue presented on this appeal is whether a *reorganization court* in a §77 proceeding has *summary jurisdiction* to enjoin a *non-judicial set-off* of claims for goods, services, and shipping losses and damages against freight charges, where such set-offs were effected prior to the Debtor's filing for reorganization. (Emphasis added)

That is not the issue in this case. Here we are dealing with the jurisdiction of the Illinois court, entertaining a plenary suit of the Petitioners, where it has subject-matter and personal jurisdiction in an action which the Court of Appeals has observed was nothing more than ordinary lawsuit. 484 F.2d at p. 951.

Besides, the classification by the Reorganization Court of the various shippers before it, 339 F. Supp. pp. 606-607, indicate factual situations different from this case and properly disposable by the exercise of summary jurisdiction.

Thompson v. Texas Mexican R. Co., 328 U.S. 134 (1946) holds merely that in reorganization matters creditors' claims are to be "reduced to judgment and may then be presented to the bankruptcy court for proof and allowance." 332 U.S. at p. 141. That was what was done in the instant case; the Illinois judgment recovered by Respondent standing as a claim in the reorganization proceeding of Penn-Central, subject to allowance on proof.

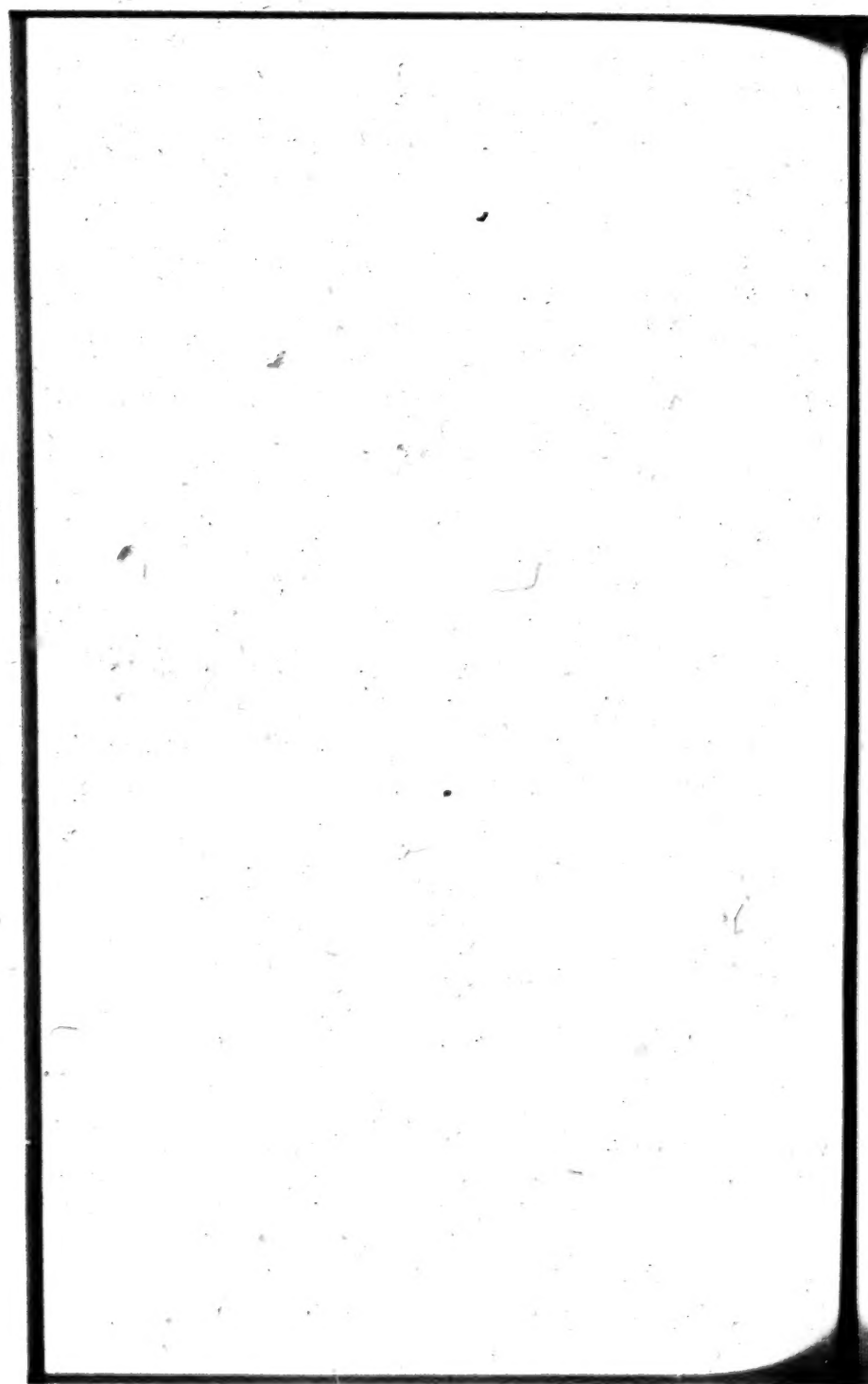
Order No. 571 of the Pennsylvania reorganization court was not binding or controlling on the Illinois court. It is submitted that there is no basis or reason to grant certiorari in the instant case.

CONCLUSION

For the foregoing reasons it is respectfully submitted that this Petition for a Writ of Certiorari should be denied.

Respectfully submitted,

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MICHAEL RODAK, JR.

IN THE

Supreme Court of the United States

October Term, 1973

No. 73-804

GEORGE P. BAKER, RICHARD C. BOND, and JERVIS
LANGDON, JR., TRUSTEES OF THE PROPERTY OF
PENN CENTRAL TRANSPORTATION COMPANY,
Debtor,

Petitioners,

v.

GOLD SEAL LIQUORS, INC.,

Respondent.

On Writ of Certiorari to the United States Court of Appeals
for the Seventh Circuit

BRIEF FOR THE PETITIONERS

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IN THE
Supreme Court of the United States

OCTOBER TERM, 1973

No. 73-804

GEORGE P. BAKER, RICHARD C. BOND, AND
JERVIS LANGDON, JR., TRUSTEES OF THE
PROPERTY OF PENN CENTRAL TRANSPORTA-
TION COMPANY, DEBTOR,

Petitioners,

v.

GOLD SEAL LIQUORS, INC.,

Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF
APPEALS FOR THE SEVENTH CIRCUIT

BRIEF FOR THE PETITIONERS

OPINIONS BELOW.

The findings of fact and opinion of the District Court for the Northern District of Illinois, entered February 18, 1972, are unreported and are printed in the Single Appendix (A35). The opinion of the Court of Appeals, entered on August 23, 1973 (A38), is reported at 484 F.2d 950.

JURISDICTION.

The judgment of the United States Court of Appeals for the Seventh Circuit was entered on August 23, 1973. A petition for certiorari was filed on November 20, 1973, and was granted January 21, 1974. This Court's jurisdiction rests on 28 U.S.C. Section 1254(1).

QUESTION PRESENTED

Did the court below err in holding that a shipper was entitled to a net judgment and consequently to effect a set-off where a railroad in reorganization sued the shipper for pre-reorganization freight charges and the shipper counter-claimed for pre-reorganization loss and damage to shipments and where the Reorganization Court had denied set-offs to such creditors in the reorganization proceedings.

STATEMENT OF THE CASE

The facts in the case are quite simple. On June 21, 1970, Penn Central Transportation Company filed a petition for reorganization under Section 77 of the Bankruptcy Act (11 U.S.C. 205). The petition was filed in the District Court for the Eastern District of Pennsylvania (Reorganization Court), under the caption "In the Matter of Penn Central Transportation Company, Debtor, No. 70-347," and on the same day the Reorganization Court entered Order No. 1 approving the petition. Paragraph 10 of Order No. 1 provided:

"10. All persons, firms and corporations, holding collateral heretofore pledged by the Debtor as security for its notes or obligations or holding for the account of the Debtor deposit balances or credits be and each of them hereby are restrained and enjoined from selling, converting or otherwise disposing of such collateral, deposit balances or other credits, or any part thereof, or from offsetting the same, or any thereof, against any obligation of the Debtor until further order of this Court." (A31-32)

On July 22, 1970, pursuant to Court Order No. 20, George P. Baker, Richard C. Bond, Jervis Langdon, Jr., and Willard Wirtz were appointed Trustees of the Debtor. The Trustees, *inter alia*, sought, as authorized by paragraph 5 of Order No. 1 (A29-30), to collect the assets of the Debtor's estate, of which one was a claim for freight charges which Gold Seal Liquors owed to the Debtor.

On December 22, 1970, the Trustees brought suit in the United States District Court for the Northern District of Illinois against Gold Seal Liquors to recover \$8,256.61 in freight charges which had accrued during a period of approximately a year and a half prior to June 21, 1970 (A4).

The cause of action arose under the laws of the United States regulating commerce, 49 U.S.C. Sections 3(2) and 6(7), and the District Court below had jurisdiction of the action under 28 U.S.C. Section 1337. Gold Seal Liquors filed a counterclaim for \$19,319.42 for loss and damage to various shipments accruing over a period of approximately two years prior to June 21, 1970 (A7-8).

The parties filed a stipulation of facts in which Gold Seal Liquors admitted its liability to the Trustees in the amount of \$6,999.76, and the Trustees acknowledged their liability to Gold Seal Liquors in the amount of \$18,016.77 (A11-14). The Trustees filed a motion for summary judgment which prayed that the Court enter a judgment for plaintiff in the amount admitted by defendant, Gold Seal, and for defendant in the amount admitted by the plaintiff Trustees (A17-18).

Previous to the institution of this action, the Reorganization Court had prohibited various bank creditors from offsetting against the Debtor (*Penn Central Transportation Co. v. National City Bank of Cleveland, et al.*, 315 F. Supp. 1281 (E.D. Pa. 1970) (Bank Setoff Case)), and had under advisement a petition of the Trustees for an order directing certain shippers to pay amounts due Debtor and prohibiting the shippers from offsetting.

After the institution of this matter, but prior to a decision by the Illinois District Court, the *Bank Setoff Case* was affirmed by the Third Circuit Court of Appeals. *In re Penn Central Transportation Co.*, 453 F.2d 520 (3d Cir. 1971), cert. den. 408 U.S. 923 (1972). Further, during the same period, the Reorganization Court entered Order No. 571 granting the Trustees' petition prohibiting certain shippers, *inter alia*, from setting off freight loss and damage claims against amounts owed the Debtor for freight transportation services. *In the Matter of Penn Central Transportation Company, Debtor*, 339 F. Supp. 603 (1972),

aff'd. 477 F.2d 841 (3d Cir. 1973), *cert. den.* — U.S. — (No. 72-1698, 42 U.S. Law Week 3213); *aff'd. sub nom. U.S. Steel Corp. v. Trustees*, — U.S. — (No. 73-94, 42 U.S. Law Week 3213) (Shippers' Setoff Case).

The Illinois District Court granted plaintiff Trustees' motion for summary judgment, but set off one judgment against the other, which resulted in a net judgment in favor of Gold Seal Liquors against the Trustees in the amount of \$11,017.01. The Court stated that restraints of setoffs by the Reorganization Court were only against extra-judicial self-help setoffs, and that in the matter before it, denial of the setoff would be inequitable (A37).

The Trustees appealed. The Circuit Court affirmed. Affirmance for the net judgment permitted Gold Seal Liquors to recover dollar for dollar on its pre-reorganization claim for loss and damage to the extent of the amount of the Trustees' admitted claim against Gold Seal, *viz.*, \$6,999.76.¹

1. Although the Circuit Court stated that Gold Seal Liquors must now submit its claim on the judgment to the Reorganization Court, it has, by affirming the net judgment, already permitted Gold Seal Liquors to recover \$6,999.76.

ARGUMENT I

THE DISTRICT COURT HANDLING THE REORGANIZATION OF THE DEBTOR HAS EXCLUSIVE JURISDICTION OVER THE PROPERTY OF THE DEBTOR AND THEREFORE THE COURT BELOW ERRED IN ENTERING A NET JUDGMENT THEREBY DISPOSING OF PETITIONERS' CHOSE IN ACTION.

Section 77(a) of the Bankruptcy Act provides in pertinent part:

"If the petition is so approved, the court in which the order is entered shall, during the pendency of the proceedings under this section and for the purposes thereof, have *exclusive jurisdiction of the debtor and its property wherever located . . .*" [Emphasis added.]

Upon approving Penn Central Transportation Company's (Debtor) petition for reorganization under Section 77 of the Bankruptcy Act (11 U.S.C. Section 205), the Reorganization Court became vested with exclusive jurisdiction over the property of the Debtor. *In re New York, New Haven and Hartford Railroad Co.*, 457 F.2d 683 (2d Cir. 1972) *cert. den.* 409 U.S. 890 (1972); *Calloway v. Benton*, 336 U.S. 132, 147 (1949); *Ex Parte Baldwin*, 291 U.S. 610.

In *Ex Parte Baldwin*, 291 U.S. 610, 615 (1934), this Honorable Court stated:

"All property in the possession of a bankrupt of which he claims the ownership passes, upon the filing of a petition in bankruptcy, into the custody of the court in bankruptcy. . . . Having possession, the Court may not only issue all writs necessary to protect its possession from physical interference, but is entitled to determine all questions respecting the same"

In the exercise of its exclusive jurisdiction over the property of the Debtor, the Reorganization Court entered Order No. 1 which, *inter alia*, enjoins setoffs (A31-32).² The setoff provisions of Order No. 1 were first tested in the *Bank Setoff Case* which was affirmed by the Third Circuit Court of Appeals. *In re Penn Central Transportation Co.*, 453 F.2d 520 (3d Cir. 1971), *cert. den.* 408 U.S. 923 (1972).

Subsequent to the *Bank Setoff Case*, in the *Shippers' Setoff Case* (339 F. Supp. 603), the Trustees petitioned the Reorganization Court for an order directing numerous shippers to pay several million dollars in freight charges due the Debtor.³ These creditors had refused to pay the freight charges except to the extent a balance might be left after they had offset against the freight charges amounts which they claimed the Debtor owed them. The Reorganization Court first concluded that the Debtor had an obligation to collect freight charges due it, and the existence of claims against the Debtor did not change this. That Court then recognized that, but for reorganization, the shippers' claims against the Debtor could be litigated in actions brought by the Debtor to collect its freight charges. Noting that the Third Circuit Court of Appeals in the *Bank Setoff Case*, *supra*, had affirmed the Reorganization Court's jurisdiction to control the exercise of setoff rights, the Reorganization

2. While a setoff or counterclaim is automatically permitted in an ordinary bankruptcy because of Section 68 of the Bankruptcy Act (11 U.S.C. § 108), it is not mandatory in reorganizations. *Susquehanna Chemical Corporation v. Producer's Bank & Trust Co.*, 174 F.2d 783 (3d Cir. 1949); *In re Penn Central Transportation Co.*, 453 F.2d 520 (3d Cir. 1971); *In the Matter of Penn Central Transportation Co.*, 477 F.2d 841 (3d Cir. 1973); see also *Lowden v. N.W. National Bank*, 298 U.S. 160 (1936); *In re Lehigh and Hudson River Ry. Co.*, 468 F.2d 430, 433 (2d Cir. 1972).

3. Respondent was not a party to this petition and the Trustees do not contend he is in violation of the Court's specific order emanating from the petition.

Court proceeded to answer the question of whether the Court should exercise its discretion to enjoin setoffs in the circumstances presented.

The Court reviewed the relevant factors and concluded that setoffs should not be permitted at this time. The relevant factors were as follows:

1. to permit the setoffs would be to discriminate against the vast majority of shippers who had paid their pre-bankruptcy freight charges in full;

2. the cash need of the reorganization must be considered. It is more consistent with the overall purposes of Section 77 of the Bankruptcy Act that shipper claims be disposed of in the proofs of claim procedure rather than that current operating revenues of the Debtor should be jeopardized by setoffs; and

3. the Trustees, in the exercise of their business judgment, in an attempt to treat all parties fairly, requested that setoffs be restrained (339 F. Supp. 603, 606 (E.D. Pa. 1972)).

The Third Circuit Court of Appeals affirmed the summary jurisdiction of the Reorganization Court and reiterated that it was in that Court's sound discretion to determine "whether or not to permit setoff or counterclaim against the Debtor's charges." (477 F.2d at 845).⁴

Despite the denial of setoffs by the Reorganization Court, and despite its exclusive jurisdiction over the property of the Debtor, the Court of Appeals for the Seventh Circuit, by affirming the entry of a net judgment in this matter, has disposed of property of the estate, viz., an admittedly valid chose in action for \$6,999.76. It has required it to be applied in partial payment of a pre-reorgan-

4. In two separate efforts to obtain review of this matter, this Court affirmed summarily and denied certiorari. See pp. 4-5, *supra*.

ization claim against the estate of the Debtor for loss or damage to freight.*

This was clearly erroneous. The Reorganization Court has exclusive jurisdiction over the property of the Debtor, including the \$6,999.76. The court below lacked power to dispose of this property. In entering the net judgment instead of granting the relief prayed for by the Trustees and entering separate judgments on petitioners' claim and respondent's counterclaim, the court below erred. The Seventh Circuit belatedly recognized that the "judgment of the Illinois court must now be submitted to the reorganization court with all other claims, to be satisfied in accordance with the appropriate orders of that court." (A40-41). However, this recognition only partially accedes to the jurisdiction of the Reorganization Court, for having affirmed the entry of a *net* judgment, it has *pro tanto* interfered with property in the exclusive possession of that Court.

The proper procedure that the courts below should have employed is evidenced in a case similar to the instant one and involving petitioners, i.e., *Trustees v. Southeastern Michigan Shippers Co-Operative Association* (B1).⁵ Here also both parties were indebted to one another, and one of the issues was whether setoff should be permitted. The Court analyzed the setoff issue thoroughly and concluded that "... this court is without power to effect a set-off

5. The Trustees do not contend that the court below lacked jurisdiction to decide the counterclaim to the extent of liquidating the claim. Section 77(j) provides that "suits or claims for damages caused by the operation of trains, . . . may be filed and prosecuted to judgment in any court of competent jurisdiction. . . ." See *Liquid Carbonic Corp. v. Erie R. Co.*, 171 Misc. 969, 14 N.Y.S. 2d 168 (1939); *Erie R. Co. v. Wm. J. Pfeil, Inc.*, 256 App. Div. 465, 11 N.Y.S. 2d 155 (1939).

6. The decision is as yet unreported. It is printed in an Addendum to this brief as a convenience for the Court and cited herein as "(B—)."

of any amounts recovered. . . ." (B15). Pursuant to Section 77(j) of the Bankruptcy Act, and in the interest of judicial economy, the Michigan District Court has permitted the counterclaim to be prosecuted and, if successful, has required that it be presented to the Reorganization Court for proof and allowance. In this regard the Michigan District Court stated:

"In essence, the bankruptcy court may modify in any way it feels necessary any right asserted against the debtor which might adversely affect the reorganization plan. The fact that it is raised in the form of a counterclaim to a suit instituted by the trustees is irrelevant. The counterclaim is not a defense to the original claim, but an independent claim which must be approached on its own merits." (footnote omitted) (B8).

The Illinois District Court failed to recognize this distinction and erred in entering net judgments. As the Michigan District Court stated:

"Even if this court may also hear defendant's counterclaim . . . , it may not satisfy that judgment out of the debtor's property, including its judgment in this suit. Once 'the claim is reduced to judgment [it] may then be presented to the bankruptcy court for proof and allowance.' *Thompson v. Texas Mexican Ry. Co.*, 328 U.S. 134, 141 (1946)." (B8).

This procedure followed by the Michigan Court accords full deference to the exclusive jurisdiction of the Reorganization Court, but at the same time is consistent with the dictates of judicial economy and efficiency. It permits liquidation of the two claims in the proceedings before it, but does not dispose of any property of the Debtor's Trustees or make any payment on claims which are within the exclusive jurisdiction of the Reorganization Court.

ARGUMENT II

IF ALLOWED TO STAND THE DECISION OF THE COURT BELOW WOULD HAVE A SERIOUS DETRIMENTAL EFFECT ON THE REORGANIZATION OF THE DEBTOR AND WOULD PERMIT INEQUITABLE TREATMENT OF CREDITORS OF THE SAME RANK.

While the amount involved in this one proceeding is relatively small, there are several other suits pending in courts in the Seventh Circuit which would obviously be governed by the decision below and, unless overturned, will result in claimants who happened to be sued in that Circuit receiving a clear preference over all other claimants with similar claims. As indicated above, considerations of practicality and judicial economy are what compelled the Trustees to liquidate their own claim in the District Court for the Northern District of Illinois. As shown by the record herein, there was a dispute as to the actual amount owing to the Trustees on their chose in action for freight charges, and it was not until the factual dispute was resolved (here admittedly by way of stipulation) that the actual amount of the chose was liquidated. In a reorganization proceeding of this magnitude, to compel the Trustees to recover on every chose in their possession in the Reorganization Court could bring the reorganization proceeding itself to a standstill.

By failing to consider properly the reorganization proceeding of the Debtor, the courts below have discriminated in favor of Gold Seal Liquors to the detriment of other creditors of the Debtor. Other loss and damage claimants are relegated to the proof of claim procedure to recover any amounts owed to them. The judgment below is grossly unfair in that it permits Gold Seal Liquors to recover

presently at least the amount of the setoff, \$6,999.76, 100 cents on the dollar. If the holding below is permitted to stand, the Trustees will be faced with a Hobson's choice. They will have to forego the attempt to recover property of the estate in other fora, which is inconsistent with principles of judicial economy and efficiency, or prosecute such actions, with the result that certain creditors will recover all or part of their pre-bankruptcy claims, while other creditors are denied that right.

It should be noted that the Reorganization Court, in denying the right of setoff, stated that such denial would be "without prejudice to the recognition of the appropriate priority of such claims in the ultimate reorganization of the Debtor" (339 F. Supp. at 608.) Thus the Reorganization Court has attempted to accommodate the needs of the Debtor in the reorganization with the claims of the creditors who are denied the right of setoff.

CONCLUSION

The decision below should be reversed with the direction that separate judgments be entered on petitioners' claim and respondent's counterclaim.

Respectfully submitted,

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ADDENDUM

**UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF MICHIGAN
SOUTHERN DIVISION.**

**Civil Action
No. 39090.**

**GEORGE P. BAKER, RICHARD C. BOND, JERVIS
LANGDON, JR., AND WILLARD WIRTZ, TRUSTEES
OF THE PROPERTY OF PENN CENTRAL TRANS-
PORTATION COMPANY, A PENNSYLVANIA CORPORA-
TION, DEBTOR,**

Plaintiffs,

v.

**SOUTHEASTERN MICHIGAN SHIPPERS CO-OP-
ERATIVE ASSOCIATION, A/K/A SEMCO, INC., A
MICHIGAN CORPORATION,**

Defendant.

Memorandum Opinion.

(Filed September 28, 1973.)

Plaintiffs (trustees of the property of Penn Central Transportation Company) sue for freight charges totaling \$22,773.19 incurred by defendant (SEMCO, Inc.) between October 10, 1969, and November 11, 1969. Defendant pleads a prior accord and satisfaction and, in the alternative, counterclaims against plaintiffs in the amount of \$20,179.80 for damages to cargo sustained on February 21, 1969, and March 3, 1969. It is these damage claims which defendant

(B1)

contents were previously set off against the freight charges now sought by plaintiffs, the difference of \$1,852.07 having been tendered and accepted on November 17, 1969.

Accord and Satisfaction.

It appears that SEMCO did try to arrange a mutual cancellation of accounts—the railroad's carriage charges against the shipper's claims for damages to cargo. Based on the facts elicited on these cross-motions for summary judgment, however, it is unclear whether these efforts came to a legally effective fruition.¹ There are genuine and material issues of fact yet to be decided on this question, and if there were no other factors involved, this case would be inappropriate for summary disposition. This result is complicated and somewhat altered by two additional facts: (1) the freight charges involved here are covered by the Interstate Commerce Act² and (2) since these claims accrued

1. "We recognize the Michigan rule that to constitute an accord and satisfaction, the tender of payment as being in full should be made in unequivocal terms so that the creditor in accepting the payment will do so understandingly. *Durkin v. Everhot Heater Co.*, 266 Mich. 508, 513, 254 N.W. 187 [1934]." *Allstate Ins. Co. v. Springer*, 269 F.2d 805, 809 (6th Cir. 1959), cert. denied, 361 U.S. 932 (1960). See also *Lafferty v. Cole*, 339 Mich. 223, 228 (1954) (creditor must be "fully informed of the condition accompanying acceptance"). This is merely a corollary to the general principle that an accord requires a meeting of the minds of the parties in an agreement to substitute one type of performance for another. See *Stadler v. Ciprian*, 265 Mich. 252, 262 (1933).

Here the evidence indicates that defendant's offer of settlement was ambiguous and equivocal. In a letter dated November 19, 1969, defendant's executive manager indicated that the off-setting of accounts and payment of the difference did not mean that SEMCO was declining payment of the freight charges, but that they would be paid as soon as the damage claims were approved by the railroad. Without further proof of the parties' intentions, this is insufficient to prove the existence (or nonexistence) of the claimed accord.

2. 49 U.S.C. § 1 *et seq.*

the railroad has entered into reorganization under the Bankruptcy Act.³

First, plaintiffs argue that whether or not the facts make out an accord and satisfaction is in the end irrelevant, for Section 6(7) of the Interstate Commerce Act⁴ absolutely prohibits and nullifies such arrangements. That section, prompted by a congressional purpose to eliminate secret preferences and kickbacks to shippers,⁵ mandates strict adherence to published tariffs.⁶ In applying this provision, the Supreme Court has held that a carrier may be compensated for its services only by payment in cash.⁷

3. Reorganization of the Penn Central Transportation Company under 11 U.S.C. § 205 was initiated by an order of the District Court for the Eastern District of Pennsylvania on June 21, 1970 [hereinafter cited as Order No. 1], approving the railroad's petition and containing various provisions concerning its continued operation. Relevant materials may be found in the Corporate Reorganization Reporter (Penn Central).

4. "No carrier, unless otherwise provided by this chapter, shall engage or participate in the transportation of passengers or property, as defined in this chapter, unless the rates, fares, and charges which the same are transported by said carrier have been filed and published in accordance with the provisions of this chapter; nor shall any carrier charge or demand or collect or receive a greater or less or different compensation for such transportation of passengers or property, or for any service in connection therewith, between the points named in such tariffs than the rates, fares, and charges which are specified in the tariff filed and in effect at the time; nor shall any carrier refund or remit in any manner or by any device any portion of the rates, fares, and charges so specified, nor extend to any shipper or person any privileges or facilities in the transportation of passengers or property, except such as are specified in such tariffs." 49 U.S.C. § 6(7).

5. See, e.g., *Atchison, T. & S.F. Ry. Co. v. Bouziden*, 307 F.2d 230, 234 (10th Cir. 1962); *Baker v. Prolerized Chicago Corp.*, 335 F. Supp. 183, 185 (N.D. Ill. 1971). See also 49 U.S.C. § 3(1) (prohibiting preferences or prejudices).

6. "The lawful rate is that which the carrier *must* exact and that which the shipper *must* pay." *Kansas City So. Ry. Co. v. Carl*, 227 U.S. 639, 653 (1913) (emphasis added).

7. *Louisville & N.R. Co. v. Mottley*, 219 U.S. 467, 477 (1911).

or by check⁸ or by way of judicial set-off against judgments due the shipper.⁹ Any form of payment containing the potential for departure from the exact letter of the tariffs (such as the supplying of goods and services in exchange for carriage)¹⁰ is prohibited.

Defendant argues that the exception for judicial set-offs, enunciated by the Court in *Chicago & N.W. Ry. Co. v. Lindell*, 281 U.S. 14 (1930), should be extended to a prior set-off of accounts (rather than judgments) concluded informally between the parties. Defendant cites no cases supporting this position. *Burlington Northern Inc. v. United States*, 462 F.2d 526 (Ct. Cl. 1972), falls squarely within the *Lindell* exception. "According to plaintiff's reading, there can be no deduction of a damage claim against transportation charges except by adjudication of a court. But that is exactly the situation we have here." 462 F.2d at 529. The same is true of *Yale Express System, Inc. v. Nogg*, 362 F.2d 111 (2nd Cir. 1966), and *Southern Pacific Co. v. Miller Abattoir Co.*, 454 F.2d 357 (3rd Cir. 1972).

On the other hand, at least two courts have squarely faced the issue of whether non-judicial set-offs are permissible under the Interstate Commerce Act, and have determined that they are not.

"Another group of shippers contend that, prior to bankruptcy, there was an agreed settlement of mutual accounts between the Debtor and the shipper, with the result that the Debtor either owes money to the shippers, or is owed much less than is now being claimed by the Trustees. . . . To the extent that the Debtor's

8. *Fullerton Lumber Co. v. Chicago, M., St. P. & P.R. Co.*, 282 U.S. 520, 522 (1931).

9. *Chicago & N.W. Ry. Co. v. Lindell*, 281 U.S. 14, 17 (1930).

10. *Chicago, I. & L. Ry. Co. v. United States*, 219 U.S. 486, 496-97 (1911).

claims against these companies were based on freight charges, it is clear under the principles set forth previously that they were incapable of being discharged either by unilateral set-offs or by mutual agreement." *In re Penn Central Transportation Co.*, 339 F. Supp. 603, 607 (E.D. Pa. 1972).

This conclusion was specifically approved by the Third Circuit:

"[One of the appellants] contends that under applicable Pennsylvania law, it extinguished its debt to the railroad by the nonjudicial set-off of a debt owed to it by the carrier Even assuming the validity of appellant's contention under Pennsylvania law, such a set-off would have been in express contravention of the Interstate Commerce Act. Indeed, the Act was so designed to prevent the kind of secret kickbacks which this type of practice could lead to." *In re Penn Central Transportation Co.*, 477 F.2d 841, 845 (3rd Cir. 1973).

The reason for distinguishing between judicial and non-judicial set-offs is obvious. In the former case, there is no adjustment until the exact value of each party's claim has been authoritatively determined; in the latter instance, there is no guarantee that the debt off-set against the freight charges is worth the amount allowed. When the set-off is judicially supervised, there is little opportunity for collusion; when it is privately arranged, there is no such assurance. In short, it is the policy of the Act to permit payment of freight charges only in a manner offering little or no opportunity for evasion of the tariff. Judicial set-offs satisfy this requirement while private arrangements do not.

As a result, the accord and satisfaction pleaded by defendant, even if convincingly established, is inadequate to

resist the trustees' cause of action. Because defendant interposes no other defenses,¹¹ plaintiffs are entitled to summary judgment for the undisputed portion of their claim—\$22,039.89—minus the \$1,852.07 previously paid. There is a genuine dispute of fact as to waybills 223588 and 228460, totaling \$733.32, which must be resolved at trial.

The Counterclaim.

The railroad's reorganization raises a second question, namely whether the defendant may nevertheless recover in this court on its counterclaim. Initially, it should be noted that its claim is contested, both as to liability and damages. There has been presented no evidence from which this court can decide the issues raised, and therefore the defendant's cross-motion for summary judgment must be denied in any event.

Under *Lindell*, this court would ordinarily be authorized to proceed to judgment on the counterclaim and off-set any recovery thereunder against plaintiff's recovery. The problem is to determine what effect the intervening reorganization may have on the defendant's cause of action. Two issues must be considered: (1) whether the action may be maintained in this court and (2) if so, whether this court is empowered to set off any recovery against that of plaintiff (i.e., in effect to execute upon the judgment).

1. *Set-off*. Taking the second point first, this court is immediately confronted with 11 U.S.C. § 205(a), which gives the bankruptcy court in a railroad reorganization "exclusive jurisdiction of the debtor and its property wherever located" "Property" in the bankruptcy setting includes a cause of action such as that asserted by

11. "The Consignee alleged the Railroad's breach both as a defense and as a counterclaim. The alleged breach, however, does not constitute a defense to the Railroad's claim for freight charges, but constitutes an independent claim. . . ." *Southern Pacific Co. v. Miller Abattoir Co.*, 454 F.2d 357, 362 (3rd Cir. 1972).

the trustees in this case¹² and any recovery granted thereunder.¹³ "Exclusive jurisdiction" is generally given a literal interpretation.¹⁴ It follows that this court can exercise jurisdiction over the bankrupt's property, including a judgment or cause of action, only to the extent permitted by the bankruptcy court.¹⁵

That court, by its order of June 21, 1970, has authorized the trustees to institute and prosecute in any court suits for the recovery or protection of its property or rights,¹⁶ and to settle or defend claims against the debtor,¹⁷ including, in their discretion, "claims for loss, damage or delay to freight and baggage"¹⁸

"[B]ut no payment shall, without further order of this Court, be made by the Debtor in respect of any such actions, proceedings or suits on claims accruing prior to the date of this order except such claims as may be permitted to be paid by this order or by other general orders hereafter entered herein, and such as constitute preferred claims under the Acts of Congress relating to bankruptcy; and no action taken by the Debtor in defense or settlement of such claims, actions, proceedings, or suits shall have the effect of establishing any claim upon, or right in, the property or funds in the possession of the Debtor that otherwise would not exist."¹⁹

12. 11 U.S.C. § 110(a) (6).

13. Meyer v. Fleming, 327 U.S. 161, 165 (1946).

14. See, e.g., In re New York N.H. & H.R. Co., 457 F.2d 683, 689 (2nd Cir. 1972); In re Imperial "400" National, Inc., 429 F.2d 671, 676-77 (3rd Cir. 1970).

15. Cf. Warren v. Palmer, 310 U.S. 132 (1940); Ex parte Baldwin, 291 U.S. 610 (1934).

16. Order No. 1, *supra*, note 3, ¶ 5.

17. *Id.*

18. *Id.*, ¶ 3B.

19. *Id.*, ¶ 5.

Thus, it appears that this court is empowered to adjudicate the plaintiffs' claim, but that it has no authority to dispose of any recovery upon that claim, whether by way of set-off or otherwise. Even if this court may also hear defendant's counterclaim (a matter yet to be decided), it may not satisfy that judgment out of the debtor's property, including its judgment in this suit. Once "the claim is reduced to judgment [it] may then be presented to the bankruptcy court for proof and allowance." *Thompson v. Texas Mexican Ry. Co.*, 328 U.S. 134, 141 (1946).

2. *Authority to Entertain Counterclaim.* The bankruptcy court has exclusive jurisdiction over not only the debtor's property, but over "any rights that may be asserted against it. These rights may be altered in any way thought necessary to achieve sound financial and operating conditions for the reorganized company, subject to the requirements of the Act." *Callaway v. Benton*, 336 U.S. 132, 147 (1949). In a railroad reorganization the class of claims included within the scope of this power is very great. "The term 'claims' includes debts, whether liquidated or unliquidated, securities (other than stock and option warrants to subscribe to stock), liens, or other interests of whatever character." 11 U.S.C. § 205(b).²⁰

In essence, the bankruptcy court may modify in any way it feels necessary any right asserted against the debtor which might adversely affect the reorganization plan. The fact that it is raised in the form of a counterclaim to a suit instituted by the trustees is irrelevant. The counterclaim is not a defense to the original claim, but an independent claim which must be approached on its own merits.²¹

20. Also, cf. 11 U.S.C. § 205(b): "The term 'creditors' shall include, for all purposes of this section all holders of claims of whatever character against the debtor or its property, whether or not such claims would otherwise constitute provable claims under this Act."

21. See note 11, *supra*.

11 U.S.C. § 108, authorizing certain set-offs and counterclaims in ordinary bankruptcy, is not binding in Chapter X corporate reorganization cases, where it could defeat the very purpose of the reorganization by depriving the debtor corporation of much-needed working capital, thus endangering its ability to continue in operation.²² In railroad reorganizations, where the public interest in survival of the enterprise is even more compelling, the reorganization court may not only enjoin set-offs,²³ but may go further and

"... enjoin or stay the commencement or continuation of suits against the debtor until after final decree; and may, upon notice and for cause shown, enjoin or stay the commencement or continuance of any judicial proceeding to enforce any lien upon the estate until after final decree: *Provided*, That suits or claims for damage caused by the operation of trains, busses, or other means of transportation may be filed and prosecuted to judgment in any court of competent jurisdiction and any order staying the prosecution of any such cause of action or appeal shall be vacated." 11 U.S.C. § 205(j).

The Penn Central reorganization court has enjoined certain set-offs,²⁴ which the parties seem to have assumed

22. *Lowden v. Northwestern National Bank*, 298 U.S. 160, 163-66 (1936); *In re Yale Express System*, 362 F.2d 111, 116-17 (2d Cir. 1966); *Susquehanna Chemical Corp. v. Producers Bank & Trust Co.*, 174 F.2d 783, 787 (3d Cir. 1949).

23. *Penn Central Transportation Co. v. National City Bank of Cleveland*, 315 F. Supp. 1281, 1283-84 (E.D. Pa. 1970), affirmed sub nom. *In re Penn Central Transportation Co.*, 453 F.2d 520, 522-23 (3d Cir. 1972).

24. "All persons, firms and corporations, holding collateral heretofore pledged by the Debtor as security for its notes or obligations or holding for the account of the Debtor deposit balances or credits be and each of them hereby are restrained and enjoined

are applicable in this case, though the assumption is a rather questionable one. This point is mooted, however, by the court's broader command that:

"All persons and all firms and corporations, whatsoever and wheresoever situated, located or domiciled, hereby are restrained and enjoined from interfering with, seizing, converting, appropriating, attaching, garnisheeing, levying upon, or enforcing liens upon, or in any manner whatsoever disturbing any portion or the assets, goods, money, deposit balances, credits, choses in action, interests, railroads, properties or premises belonging to, or in the possession of the Debtor as owner, lessee or otherwise, or from taking possession of or from entering upon, or in any way interfering with the same, or any part thereof, or from interfering in any manner with the operation of said railroads, properties or premises or the carrying on of its business by the Debtor under the order of this Court and from commencing or continuing any proceeding against the Debtor, whether for obtaining or for the enforcement of any judgment or decree or for any other purpose, provided that suits or claims for damages caused by the operation of trains, buses, or other means of transportation may be filed and prosecuted to judgment in any Court of competent jurisdiction"

Because of the bankruptcy court's exclusive jurisdiction over such matters, that mandate is binding upon this court.

24. (Cont'd.)

from selling, converting or otherwise disposing of such collateral, deposit balances or other credits, or any part thereof, or from offsetting the same, or any thereof, [sic] against any obligation of the Debtor, until further order of this Court." Order No. 1, *supra* note 3, ¶ 10 (footnote omitted).

25. *Id.*, ¶ 9.

Thus the ultimate issue is whether the proviso in subsection (j) of the statute, incorporated verbatim in the court's order, applies to defendant's counterclaim. If it constitutes a claim "for damages caused by the operation of trains, busses, or other means of transportation," it is cognizable in this court. If not, it falls within the scope of the order and its prosecution here is effectively enjoined.

There is relatively little case law interpreting the proviso, and what there is is either contradictory or inconclusive. Certainly "[t]he language of the proviso in § 77(j) is sufficiently broad to include all tort or contract claims whatsoever that arise from the operation of the trains or busses of the debtor." 5 *Collier on Bankruptcy* ¶ 77.12 at 516 (14th ed. 1970). Such a literal reading of the statute would clearly place SEMCO's counterclaim within the proviso. On their facts, several cases from the New York courts appear to support this result. See *Erie R. Co. v. William J. Pfeil, Inc.*, 11 N.Y.S.2d 155, 256 App. Div. 465 (1939) (counterclaim for damage to shipment of beans caused by salt in car held to be within proviso; counterclaim for breach of contract to construct a side track was outside proviso); *Yerckes-Eichenbaum, Inc. v. McCarthy*, 35 N.Y.S.2d 527, 264 App. Div. 403 (1942) (action for breach of contract of carriage within proviso); *Liquid Carbonic Corporation v. Erie R. Co.*, 14 N.Y.S.2d 168, 171 Misc. 969 (1939) (damage to cargo caused by failure to provide proper unloading facilities held to be within proviso). On the other hand, an opinion of the Seventh Circuit Court of Appeals of about the same vintage discusses the proviso at length, and concludes that Congress intended only to exempt personal injury claims. *In re Chicago & E. I. Ry. Co.*, 121 F.2d 785, 789 (7th Cir. 1941), cert. denied sub nom. *Chicago & E. I. Ry. Co. v. Gourley*, 314 U.S. 653 (1941). Two other federal courts have effectively avoided the issue in personal injury cases, which are uniformly recognized as

falling within the proviso. *Munnelly v. Farrell*, 317 F. Supp. 329 (S.D.N.Y. 1970); *Rodabaugh v. Denny*, 24 F. Supp. 1011 (S.D.N.Y. 1938). Finally, one other federal court seemed in passing to endorse the personal injury restriction, but went on to hold that a penalty for violation of the Safety Appliance Act is outside the proviso without ever defining its exact scope. *United States v. Dorigan*, 236 F. Supp. 106, 108 (E.D.N.Y. 1964).

It seems a sound rule of construction to adopt the simplest, most obvious interpretation of statutory language, unless there are clearly shown, persuasive reasons for doing otherwise.²⁶ A court may reasonably adopt a narrower or broader construction when to do so would better effectuate legislative intent.²⁷ This imperfectly expressed intent may have been actual (often discovered in legislative history) or it may be implied (a euphemism for the judicial rounding off of a law's sharp corners). But however the burden of justifying a non-literal interpretation is formulated, it has not been satisfied here. There is no legislative history to indicate that Congress intended something other than what it appeared to say. There is no evidence of overriding policies or dysfunctional effects which would permit this court to conclude that Congress should or would have intended something else, and to impute to it such intent *nunc pro tunc*.

26. "True, courts in the interpretation of a statute have some scope for adopting a restricted rather than a liberal or a usual meaning of its words where acceptance of that meaning would lead to absurd results, . . . or would thwart the obvious purpose of the statute. . . . But courts are not free to reject that meaning where no such consequences follow and where, as here, it appears to be consonant with the purposes of the Act as declared by Congress and plainly disclosed by its structure." *Helvring v. Hammel*, 311 U.S. 504, 510-11 (1941).

27. "It is well established, however, that a meaning not conveyed by the literal language may be given in order to carry out the legislative intention, if the words used will bear such meaning." *United States v. Breenan*, 214 F.2d 268, 270 (D.C. Cir. 1954), cert. denied, 348 U.S. 830 (1954).

Indeed, to the extent there are such factors, they weigh in favor of a literal reading of the proviso. First, it would not alter the bankruptcy court's power to rule on the allowance of such claims, thus producing no interference with any part of the reorganization plan (which is the primary *raison d'être* for this section of the statute).

Second, the policy behind the subsection (j) proviso itself appears to be similar to that behind 28 U.S.C. § 959, permitting suit without leave of the bankruptcy court respecting acts or transactions of the trustees in "carrying on" the debtor's business. Referring to a predecessor of that section, the Supreme Court observed that:

"This act abrogated the rule that a receiver could not be sued without leave of the court appointing him, and gave the citizen the unconditional right to bring his action in the local courts, and to have the justice and amount of his demand determined by the verdict of a jury. He ceased to be compelled to litigate at a distance, or in any other forum, or according to any other course of justice, than he would be entitled to if the property or business were not being administered by the Federal court.

"The object of the section is manifest, and it is equally plain that that object would be open to be defeated if the receiver could remove the case at his volition. The intention to permit this to be done cannot reasonably be imputed to Congress, and, moreover, such a right would be inconsistent with the general policy of the act." *Gableman v. Peoria, D. & E. Ry. Co.*, 179 U.S. 335, 338 (1900).

Such a rationale suggests no basis for distinguishing between claims for property damage and those for personal injury. Judge Patterson, in the *Rodabaugh* case, reached a similar conclusion in an analogous situation:

"In a very broad sense every action against a railroad company wherein money damages are demanded is an action for 'damages caused by the operation of trains, busses, or other means of transportation.' The primary business of a railroad company is to operate trains, and all its activities are incidental to the operation of trains. The words of the proviso are not to be construed so broadly; nor on the other hand, should they be construed so narrowly as to defeat the purpose of Congress in enacting the proviso. Congress doubtless had in mind the fact that the district court in charge of reorganization might be a long distance from the court in which an action for damages might be brought, and that the obtaining of consent of the court in charge of reorganization might be a hardship on a claimant. This is a factor in favor of a liberal interpretation of the proviso. There is no apparent reason for a distinction between the case of a plaintiff who is struck by a moving train and the case of a plaintiff who was injured by the collapse of a scaffold while working as an employee of the railroad. I am of opinion [sic] that the present case is one 'for damages caused by the operation of trains, busses or other means of transportation' and that the prosecution of the action in the usual manner has not been restrained by the reorganization court." 24 F. Supp. at 1012.

Finally, it must be remembered that defendant presses its claim in this court only in response to one initiated here by the trustees themselves. To hear the plaintiffs' case but not the defendant's, when both might easily be disposed of in one action, seems not only an uneconomic allocation of judicial resources but also an unduly harsh and useless result. As a general rule, statutes should be construed so

as to avoid the imposition of such arbitrary and meaningless hardships.²⁸

For these reasons, summary judgment will enter in favor of plaintiffs for the undisputed portion of their claim. The remainder of their claim, as well as defendant's counterclaim, may be prosecuted in this court. However, this court is without power to effect a set-off of any amounts recovered pursuant thereto.

An appropriate order may be submitted.

JOHN FEIKENS,
United States District Judge.

DATED: DETROIT, MICHIGAN
SEPTEMBER 28, 1973.

28. "The courts draw back from the construction of an ambiguous statute that would lead to unjust results, just as nature draws back from the consistency of one of its laws that would encase in ice fish at the bottom of a river." *Voris v. Gulf-Tide Stevedores*, 211 F.2d 549, 552-53 (5th Cir. 1954), cert. denied, 348 U.S. 823 (1954).

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IN THE
SUPREME COURT OF THE UNITED STATES
OCTOBER TERM, 1973

No. 73-804

GEORGE P. BAKER, RICHARD C. BOND, and JERVIS
LANGDON, JR., TRUSTEES OF THE PROPERTY
OF PENN CENTRAL TRANSPORTATION COMPANY,
Debtor,

Petitioners,

vs.

GOLD SEAL LIQUORS, INC.,

Respondent.

On Writ of Certiorari to the United States Court
of Appeals for the Seventh Circuit.

BRIEF FOR THE RESPONDENT

OPINIONS BELOW

The memorandum opinion and order of the District Court for the Northern District of Illinois, entered March 16, 1972, is unreported and is printed in the Single Appendix (A 35-37). The opinion of the Court of Appeals for the Seventh Circuit, entered August 23, 1973 (A 38-41), is reported at 484 F.2d 950.

JURISDICTION

The judgment of the Court of Appeals was entered August 23, 1973. The petition for certiorari was filed November 20, 1973 and was granted January 21, 1974. The jurisdiction of this Court rests on 28 U.S.C. Section 1254(1).

QUESTION PRESENTED

Whether the orders of the Reorganization Court barring setoffs by creditors of the Debtor precluded the District Court below in a plenary suit brought by Petitioners, from offsetting against the amount found due Petitioners the greater amount found due Respondent and entering a net judgment in favor of Respondent.

STATEMENT OF THE CASE

Petitioners commenced a plenary action on December 22, 1970 in the United States District Court for the Northern District of Illinois to recover unpaid freight charges. Respondent counterclaimed for losses incurred from damage to shipments of merchandise bought by Respondent but delivered by Penn Central. Respondent's damages were almost three times the amount claimed by Petitioners.

The District Court, on the basis of stipulated facts, found Petitioners indebted to the Respondent for \$18,016.77, the Respondent indebted to Petitioners for \$6,999.76, and entered judgment in favor of Respondent for \$11,017.01.

Petitioners appealed to the Court of Appeals for the Seventh Circuit which affirmed the District Court, holding that Order No. 571 of the Reorganization Court, set forth as an Addendum to this brief, did not require the District Court to withhold the full exercise of its jurisdiction in Petitioners' plenary suit in that forum.

ARGUMENT I

THE REORGANIZATION COURT COULD NOT BY SUMMARY JURISDICTION BAR THE DISTRICT COURT FROM GIVING EFFECT TO DEFENDANT'S COUNTERCLAIM.

The Trustees in Argument I of their brief argue that the "exclusive jurisdiction" of the Reorganization Court over the property of the Debtor extends the application of the Reorganization Court's order, entered in summary proceedings, to plenary suits wherever they may be brought.

The exclusive jurisdiction of the Debtor's property, which is summary in nature, pertains only to property over which the Court has actual or constructive possession. The test of this jurisdiction is not title or right, but possession of the Debtor at the time of the filing of the petition. *Thompson v. Magnolia Petroleum Co.*, 309 U.S. 478, 481 (1940).

The bankruptcy court is without summary jurisdiction to determine adverse claims to property not in the possession of the debtor or its trustees, and an action to recover on such claims may be brought only in courts where the bankrupt-debtor could have litigated the question. *First National Bank of Chicago v. Chicago Title & Trust Co.*, 198 U.S. 280, 289 (1904).

Property or money held adversely to the bankrupt-debtor can only be recovered in a plenary suit and not by summary proceeding. *Gailbraith v. Valle*, 256 U.S. 46 (1920); *First National Bank of Chicago v. Chicago Title & Trust Co.*, *supra*; *Louisville Trust Co. v. Cominger*, 184 U.S. 18 (1901); cf. *May v. Henderson* 268 U.S. 112, 115 (1925).

The assertion of a right of setoff deprives the Reorganization Court of summary jurisdiction to determine the issues raised and requires a plenary hearing in the appropriate form. Where a respondent asserts a substantial claim of setoff against that which is sought by the trustee, an adverse claim is raised that can be adjudicated only in a plenary action. *In re Chicago and Northwestern Ry.*, 86 F.2d 508 (7th Cir. 1936). 4 Collier Bankruptcy (14th Ed.) ¶68.20 [4] p. 945. Nor is a claim by the debtor against a third person "property" of the debtor which will support summary proceedings in the reorganization court to collect the debt. *Duda v. Sterling Mfg. Co.*, 178 F.2d 428, 435 (8th Cir. 1949); *In re Standard Gas & Electric Co.*, 119 F.2d 658, 661-62 (3rd Cir. 1941); *Thompson v. Terminal Shares*, 104 F.2d 1, 9 (8th Cir. 1939) cert. denied 308 U.S. 559 (1939); *In re Roman*, 23 F.2d 556 (2nd Cir. 1928).

Only if a third party has money, which is the property of the debtor which it merely colorably retains, can the Reorganization Court exercise summary jurisdiction. *Taubel-Scott-Kitzmiller Co., Inc. v. Fox*, 264 U.S. 426 (1923); *May v. Henderson*, 268 U.S. 111, 115 (1925). Here the position of the defendant Gold Seal Liquors, Inc. has at all times been that of an adverse claimant with a substantial and not merely colorable defense. The claim of the debtor, constituting a chose of action in this case, cannot be said to be property not subject to an adverse claim and hence within the reach of the summary procedure of the Reorganization Court.

The comments of Judge Learned Hand in *In re Roman*, 23 F.2d 556 (2d Cir. 1928) at p. 558, reversing an order entered summarily, directing payment of the bankrupt's debtor are pertinent;

"Nobody can maintain that, before the payment is made, the bankrupt has any property in the syndicate's hands. Even though its refusal were no better than colorable, its property remained its own; it had only broken its promise, and like any other promisor, was liable to an action for damages. Thus, not only is the order a decree of specific performance, where no such remedy exists, but it ignores the distinction between the obligation to perform and the consequences of performance. It would not be permissible to collect even a bank deposit due a bankrupt by these means. So far as possession can be imputed to such property at all, it is confined to the rights of the bankrupt to enforce the promise. The trustee must proceed as the bankrupt must have proceeded, in a court having competent jurisdiction in such causes."

The distinction between the Reorganization Court's power to decide conflicting claims of ownership of the Debtor's chose in action, of which none exist in this case, and the power to adjudicate the claim of the Debtor against Gold Seal, which it did not have, is expressed in *In re Lehigh and Hudson River Ry.*, 468 F.2d 830 (2d Cir. 1972). The reorganization court in that matter entered an order approving the petition for reorganization of the Lehigh Railroad. Paragraphs 10 and 11 of the order were substantially the same as Paragraphs 9 and 10 respectively, of Order No. 1 entered in the Penn Central reorganization (A 31). Penn Central nevertheless, in disregard of the orders of the reorganization court, set off and applied the sums it was obligated to pay Lehigh against Lehigh's indebtedness to it. In response to an order to show cause, Penn Central asserted that the facts relating to the account presented "a substantial adverse claim as to the Petitioner's entitlement to the amount sought, and the Court is therefore without jurisdiction to enter the order sought in a summary proceeding." On

appeal by Penn Central, from an order enjoining and restraining the Penn Central trustees from failing to honor drafts submitted by Lehigh for interline freight balances and overcharge claims, the order was vacated, without prejudice to the bringing of a plenary suit. Chief Judge Friendly at page 433 first corrected a misconception of the Lehigh Railroad, which Penn Central appears to share in this case:

"At the outset, it is well to correct a misconception resulting from Lehigh's reliance on the statement in 2 Collier, Bankruptcy ¶23.05 [4], at 485 (1971), cited by the district court:

'Where the character of the property is such that it is not capable of tangible or actual physical custody, constructive possession will suffice to confer summary jurisdiction upon the bankruptcy court regarding such property.'

"The discussion makes clear that this statement refers to conflicting claims of the bankrupt and others to the *ownership* of such intangibles; in such cases the rule with respect to choses in action is the same as that with respect to tangible property. But, as is explained in the final sentence of the subsection, *id.* at 489-90, and the cases cited in fn. 33, the bankruptcy court does not have summary jurisdiction to *enforce* a chose in action against the bankrupt's obligor, even when the bankrupt's rights seem clear. Judge Learned Hand made the distinction, with his customary clarity, in *In re Roman*, 23 F.2d 556 (2 Cir. 1928)."

Judge Friendly further noted on page 434:

"... The injunction against setoff is strong medicine. With some insolvent railroads in truly desperate conditions it may mean that the holder of a claim, who would have had the finest kind of security in ordinary bankruptcy, will be totally deprived of it since even

the priority accorded by *In re New York, N. H. & H. R. R. Co.*, 147 F.2d 40 (2 Cir.), cert. denied, *Commonwealth v. New York, N. H. & H. R. Co.*, 325 U.S. 884, 65 S.Ct. 1577, 89 L.Ed. 1999 (1945), may prove to be worthless. Phrasing the question in a case like this in terms of a violation of the order approving the petition should not veil the reality that, in practical effect, the reorganization court is ordering an obligor to pay something which he has substantial grounds for contending he no longer owed when the petition was approved."

Ex Parte Baldwin, 291 U.S. 610, 618 (1934) holds that the exclusive jurisdiction of the bankruptcy court is determined by the "main purpose" of the suit.

The main purpose of the action below was to collect freight charges from the defendant shipper who was outside the jurisdiction of the reorganization court and who could be joined only in a plenary suit. The jurisdiction of the reorganization court was at best concurrent and not exclusive, though it is questionable whether the Reorganization Court ever had jurisdiction over Gold Seal to collect the freight claim. The amount and extent of the Debtor's claim against Gold Seal cannot be determined without considering the shipper's counterclaim. The counterclaim meets squarely the claim for which the debtor sought judgment below.

This court said in *Thompson v. Texas Mexican Ry.*, 328 U.S. 134 (1946) at 138, that litigation restricted to the amount due under a contract, expressed or implied, does not interfere with the administration of the estate. Neither did the judgment entered below have such an effect, for any excess of the counterclaim over the amount of the debtor's claim must be presented to the bankruptcy court for proof and allowance.

Had Gold Seal consented in any way to the jurisdiction of the Reorganization Court, the Trustees' position would be stronger. It cannot be said, however, that Gold Seal was within the summary jurisdiction of the Reorganization Court. Gold Seal never filed a claim in the reorganization proceeding, though a claim was filed by Penn Central on behalf of Gold Seal on the basis of the amount of the shipper's freight claims as shown on the records of the Debtor as of February 1, 1971. Jurisdiction to adjudicate and collect the Debtor's freight claim against Gold Seal was acquired only by the District Court for the Northern District of Illinois in the plenary suit commenced by the Trustees.

The Trustees' position is an attempt to extend summary jurisdiction over courts adjudicating plenary suits where such suits are required for the collection of the Debtor's accounts receivable. The summary jurisdiction of the Reorganization Court is defined and limited by the Bankruptcy Act, and neither the Reorganization Court nor the Trustees appointed by it can go beyond the limitations therein prescribed.

ARGUMENT II

THE ORDERS OF THE REORGANIZATION COURT BY THEIR TERMS DID NOT BIND THE DISTRICT COURT FROM ENTERING ITS JUDGMENT.

Both the pertinent provisions of Order No. 1, paragraphs 9 and 10 (A 31) and Order No. 571, (1a)¹ did not operate to restrain judicial action in giving effect to counterclaims adjudicated in plenary suits. Both orders are directed against non-judicial setoffs, of the kind sought to be avoided in the cases cited by the Trustees. The distinction between non-judicial setoffs by creditors

resorting to self-help and the action of the District Court for the Northern District of Illinois, is crucial.

This distinction is set forth at length in the *South-eastern Michigan Shippers Cooperative* case, (Petitioner's Brief, p. (B 5), and is relevant to an analysis of the orders of the Reorganization Court which the Trustees claim were erroneously disregarded by the District Court below.

The Trustees have cited at page 7 of their brief the so-called Shipper's Set-Off case, *In re Penn Central Transportation Co.*, 339 F. Supp. 603 (E.D. Pa. 1973), affirmed 477 F.2d 841 (3d Cir. 1973). The same decision is cited by the Michigan court (B 9) in support of the proposition that the Penn Central Reorganization Court may and had power to enjoin or prevent another District Court from setting off one judgment against another. A careful examination of both opinions indicates that the case is not authority for the sweeping rule attributed to it.

In that case the Trustees filed a petition in the Reorganization Court for an order directing certain shippers to pay amounts due the Debtor. The Court noted first two principal issues raised by the petition—the extent of the Court's summary jurisdiction to control the right to resort to the remedy of set-off, assuming the existence of jurisdiction under the circumstances, the propriety of continuing the existing restraints against set-off. The Court found first under the circumstances the existence of summary jurisdiction over choses in action because of the lack of a substantial dispute concerning the ownership of the chose in action.

¹The order entered pursuant to the Reorganization Court's opinion in 339 F. Supp. 603 is not reported. It is printed as an Addendum to this brief, page 1a hereof.

The Court characterized the various respondent shippers before it in the proceeding and placed them into four categories:

The first category consisted of shippers who allegedly overpaid bills or mistakenly paid erroneous or duplicate bills. The Court found no summary jurisdiction as to these parties without their consent.

The second class consisted of shippers who contended that the debtor retained the proceeds of salvaged goods. Summary jurisdiction was not found here.

The third class consisted of shippers who contended that there was an agreed settlement of mutual accounts between the debtor and the shipper. As to these the Court found summary jurisdiction and stated that the off-setting accounts of these shippers were incapable of being discharged by unilateral set-off or by mutual agreement.

The fourth group of respondents were not shippers but companies which exchanged goods or services with the debtor not involving the carriage of freight where there was alleged the existence of contractual arrangements under which the parties would from time to time net out mutual debts and credits. As to these parties the Court found it lacked summary jurisdiction.

In none of these classes can the present defendant Gold Seal Liquors, Inc. be placed. Aside from the fact that Gold Seal was not only not before the Court and was not bound therefore by Order 571, it could not be said to belong to any classification of creditors made by the Court in its opinion.

One should examine the actual order entered on January 31, 1972, the so-called "Order 571," to determine its scope without regard to the dicta in the District Court's

opinion delivered simultaneously with the entry of the order. The order consists merely of one paragraph¹, and reads simply that all persons, firms and corporations served with a copy of said petition are enjoined until further order of the court from setting off or attempting to set off obligations due and owing to the debtor on account of charges for services of carriage any claim or claims which they may have against the debtor arising prior to June 21, 1970. It should be noted first that the order applies only to persons, firms and corporations served with a copy of the petition. Gold Seal Liquors was not so served or named therein. It should be further and finally noted that the court's injunction was against setting off or attempting to set off obligations due and owing to the debtor by the exercise of self-help, by non-judicial set-off, and not by the maintenance and prosecution or even an allowance of a counterclaim in a plenary judicial proceeding. The Reorganization Court should not be charged with an attempt to enjoin all courts from entertaining counterclaims whether or not jurisdiction exists. Such an attempt would be an unwarranted and ineffectual attempt to extend the jurisdiction of the Reorganization Court, unsupported by the Act of Congress.

That such is not the case is indicated by the characterization of the holding by the Court of Appeals for the Third Circuit, 477 F.2d 841 (3d Cir. 1973).

At page 843 of 477 F.2d, Chief Judge Seitz stated:

"The basic issue presented on this appeal is whether a reorganization court in a §77 proceeding has *summary jurisdiction to enjoin a non-judicial set-off* of claims for goods, services, and shipping losses and damages against freight charges, where such set-offs

¹ See Addendum to Respondent's brief.

were effected prior to the Debtor's filing for reorganization." (Emphasis supplied).

The matter before this Court involves not a non-judicial set-off but the allowance and recognition of the defendant's counterclaim by the District Court in Illinois in the plenary action brought by the Trustees in that forum.

The Trustees apparently place great weight on the memorandum opinion of the District Court for the Eastern District of Michigan, set forth in full in their brief here (B1-B5, incl.), in the case between the Trustees as plaintiffs and *Southeastern Michigan Shippers Co-Operative Association* as defendant. That opinion should not be controlling here for reasons hereinafter set forth.

The Michigan court's opinion is divided into two parts, one dealing with the defense of accord and satisfaction (B1-B6) and the balance (B6-B15) treating the matter of the defendant's counterclaim. No mention need be made of the first part of the opinion except to note the recognition by the Michigan court at page B5 of the distinction between judicial and non-judicial set-offs.

In considering the question of the defendant's recovery on its counterclaim, the Michigan court first decided that it could not allow any recovery on the counterclaim for reasons which do not appear to be significant. The court mentioned first the provisions of 11 USC Section 205 (a) which granted to the court approving the petition for reorganization as property filed, "exclusive jurisdiction of the debtor and its property wherever located . . ." From this the court found in paragraph 5 of the order approving the petition (Order No. 1) a prohibition against allowing the shipper's counterclaim, if proved, to affect any judgment entered on behalf of the debtor. At the outset it must be noted that the claim of the debtor against the

shipper in *Southeastern* was undisputed, whereas the amount claimed by the Trustees against Gold Seal Liquors, Inc. was in dispute (Petitioner's brief, p. 11). The dispute as to the amount owed and the amount claimed by Gold Seal from Penn Central in this case raised an adverse claim as to any chose in action consisting of Penn Central's claim against Gold Seal, thus requiring adjudication in a plenary suit.

Paragraph 5 of Order No. 1 of the Reorganization Court authorizes the Debtor Penn Central to institute or prosecute suits in other courts to liquidate, compromise, adjust or make settlement of its claims and to defend, liquidate and settle suits against it. Paragraph 5 further prohibits the Debtor from making any payment pursuant to any court order or settlement without further order of the Reorganization Court. Paragraph 5 of Order No. 1 does not restrict a district court having jurisdiction of the parties and of the subject matter in a plenary suit from proceeding to adjudicate the issues and entering a judgment as the District Court in this case did below.

The Michigan court then decided that the counterclaim could be adjudicated but that any judgment on the counterclaim could not be applied against any amount found to be due Penn Central from the shipper. The Michigan court felt that it was precluded from setting off the counterclaim by paragraph 9 of Order No. 1 of the Reorganization Court. Actually, all Order No. 1 purports to do in this regard, is to restrain individuals within the summary jurisdiction of the court from interfering with the property of the Debtor (paragraph 9) or resorting to self-help by foreclosing on collateral or setting off claims against the Debtor (paragraph 10). If the order

sought to bind other courts having plenary jurisdiction over adverse claims, it is submitted that Order No. 1 did not have such effect.

The Reorganization Court in Philadelphia is without power to control by its order the District Court in Illinois in the adjudication of a plenary suit in the Illinois court.

The question of the effect of an adverse claim on the Debtor's chose in action is not treated in the Michigan opinion. An adverse claim, made in good faith, operates to entitle the adverse claimant to a hearing in a plenary suit rather than to be subjected to a decision by summary jurisdiction of the reorganization court.

Order No. 571, insofar as it could be said to have been intended to bind the Illinois court, or other courts entertaining plenary suits, and there is no indication that such was the intention, would not be a proper or reasonable exercise of summary jurisdiction.

The jurisdiction of the bankruptcy court is not exclusive if plenary jurisdiction exists. The Reorganization Court could not enforce its order against this shipper by proceedings in that court on the claim.

The right of set-off is not inapplicable, as a matter of law, in reorganization proceedings. The ultimate determination is based upon the equities involved under the particular fact situation presented. The Trustees in this case have presented little evidence which would justify a court to determine the facts upon which that necessary legal conclusion must be based that set-off should be denied.

In *Lowden v. Northwestern Nat'l. Bank & Trust Co.*, 298 U.S. 160 (1936), the Court held that the provisions of §68 of the Bankruptcy Act recognizing the act of set-

off in proceedings under the Act do not apply automatically in §77, Reorganization Proceedings. The Court mentioned various factors which must be considered in determining if a creditor is to be denied the right of set-off, or if the general equity and bankruptcy rule allowing set-off is to be followed. Although the Court stated that §68 does not automatically apply in reorganization proceedings, it did not hold that §68 never applies to reorganization proceedings; on the contrary, the Court made clear that if set-off was not allowed, it would result in an exception to the general rule in equity and bankruptcy proceedings.

In *Susquehanna Chemical Corp. v. Producers Bank & Trust Co.*, 174 F.2d 783 (3d Cir. 1949) the Court concluded that whether the right of set-off applies in reorganization proceedings under Chapter X depends upon the facts presented and the equities of the particular case. *Chase Nat'l Bank v. Lyford*, 147 F.2d 273 (2d Cir. 1945) held that the right of set-off exists in §77 unless the creditor is estopped to assert this right against certain priority creditors.

The right of a creditor to effect a set-off is well founded in the common law. Section 68 recognizes the injustice which would result if a creditor is compelled to pay in full his debt to the estate while being limited to a percentage payment of his claim against the Debtor. See 4 Collier Bankruptcy (14th Ed.) ¶68.02 (1), p. 853. The hardship and inequity of such a procedure is obvious and the effect of such a rule is apparent. The enforcement of such a doctrine might well not result in the rehabilitation of the debtor but would nevertheless cause severe financial damage to those creditors who are subjected to substantial losses for the benefit of other creditors of the

debtor. To employ such an extraordinary remedy the trustees must demonstrate clearly and unequivocally the need that such drastic relief be had, outweighing the obvious harm to the shipper. This, the trustees have not done, especially since no feasible plan for the resuscitation of the Debtor has been brought forth after forty-five months of reorganization proceedings.

ARGUMENT III

THE JUDGMENT OF THE DISTRICT COURT IS PROPER, JUST AND EQUITABLE UNDER THE FACTS OF THIS CASE.

The Trustees portend the most serious consequences if the decision of the Court of Appeals below is not overturned. Specifically, they state that there are "several other suits pending in the courts of the Seventh Circuit" which would be governed by the decision below, which unless reversed, would result in claimants sued in the Seventh Circuit "receiving a clear preference over all other claimants with similar claims."

An examination of the files of both of the Office of the Clerk of the United States District Court for the Northern District of Illinois at Chicago and the Office of the Clerk of the Circuit Court of Cook County, Illinois, also located at Chicago, indicates at most three involving counterclaims cases, two in the Federal Court, only one of which has a substantial counterclaim pleaded and one in the Circuit Court of Cook County. Of the two cases in the District Court, one is in the process of removal to Pennsylvania. It is hard to imagine the serious consequences that will result from the affirmance of the decision of the court below. The Trustees further state that "considerations of practicality and judicial economy" are what compelled them to bring the plenary suit in Illinois.

They then state that "there was a dispute as to the actual amount owing to the Trustees on their chose in action for freight charges", thus indicating a substantial adverse claim requiring adjudication in a plenary suit. The Trustees finally plead that to compel them to recover on every chose in their possession in the Reorganization Court could bring the reorganization proceeding itself to a standstill. The Trustees have the right to litigate in the Reorganization Court where summary jurisdiction exists. Where it does not exist, as in this case, they have no alternative but to bring plenary suits to collect receivables due the Debtor.

In considering whether the judgment recovered by the defendant against the Debtor in the District Court of \$11,017.71 should stand, it should be noted that the Debtor is liable for damages to the defendant in an amount more than twice the amount sued for, which at the very least should be applied as a set-off to reduce the claim.

The Trustees argue that the District Court's action below created a preference, discriminatory to other creditors, is similar to the argument advanced by the railroad in *Chicago & Northwestern Ry. v. Lindell*, 281 U.S. 14 (1930), that allowing a counterclaim would be a discrimination in favor of a counterclaiming shipper, a collection greater or less or of different compensation than the rates and charges for shipment specified by the carrier in its tariffs. The Court rejected that argument and said that the practice of determining claims of shippers for loss or damage in suits brought by carriers to collect transportation charges was not repugnant to the rule prohibiting the payment of such charges otherwise than in money, that adjudication in one suit of the respective claims of plaintiff and defendant was the practical equiva-

lent of charging a judgment obtained in one action against that secured in another, and that neither was to be distinguished from payment in money. 281 U.S. 17. So in this case the crediting of the amount owed by the shipper against the amount owed by the Debtor is indistinguishable from payment in money by the shipper of the actual amount owed.

The Trustees complain here that if the judgment of the Court of Appeals is affirmed, that they will be faced with a "Hobson's choice," which metaphorically is no choice at all, when seeking to proceed in plenary actions against shippers to whom Penn Central is indebted in an amount greater than the amount of the Railroad's claim. Clearly, the Trustees have a choice in such a situation as any litigant does, namely, to proceed and litigate all matters including those of counterclaim, recovering what they may, or to await the filing of claims by the shippers and litigating the shipper's claims and their own off-setting claims against the shipper's in summary proceedings in the Reorganization Court. In the absence of a filed claim by a shipper, or consent by a shipper to the summary jurisdiction of the Reorganization Court, the Trustees must proceed by a plenary suit, as Congress has so prescribed.

It is a dubious preference which the defendant here is charged with receiving at the hands of the courts below, one, which the defendant Gold Seal Liquors, Inc. would gladly have foregone and one, which is solely the result of the extensive injury inflicted on the shipper by Penn Central. The Trustees should not be permitted to inflict further injury and damage to the shipper. Gold Seal has suffered a sufficient penalty for having patronized Penn Central for the carriage of freight in the period of the carrier's decline.

CONCLUSION

The decision of the Court of Appeals affirming the judgment of the District Court should be affirmed.

Respectfully submitted,

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ADDENDUM

Order No. 571

AND NOW, this 31st day of January, 1972, it is Ordered that the petition of the Trustees for an order directing shippers to pay amounts due Debtor (Document No. 400) is GRANTED IN PART, and all persons, firms and corporations served with a copy of said petition are enjoined, until further order of this Court, from setting off or attempting to set-off against obligations due and owing to the Debtor on account of charges for services of carriage any claim or claims which they may have against the Debtor, arising prior to June 21, 1970, but any such claim or claims may be filed and proved in accordance with Order No. 164 in this proceeding. This Order shall be deemed to be without prejudice to the right of any such shipper to claim such priority as may be proper.

JOHN P. FULLAM
J.

(Slip Opinion)

NOTE: Where it is feasible, a syllabus (headnote) will be released, as is being done in connection with this case, at the time the opinion is issued. The syllabus constitutes no part of the opinion of the Court but has been prepared by the Reporter of Decisions for the convenience of the reader. See *United States v. Detroit Lumber Co.*, 200 U.S. 321, 337.

SUPREME COURT OF THE UNITED STATES

Syllabus

BAKER ET AL., TRUSTEES IN REORGANIZATION v. GOLD SEAL LIQUORS, INC.

CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR
THE SEVENTH CIRCUIT

No. 73-804. Argued April 23, 1974—Decided June 17, 1974

Petitioners, trustees of a railroad in a § 77 reorganization proceeding, brought suit for freight charges against respondent shipper, and respondent counterclaimed for cargo loss and damage. The District Court granted petitioners' motion for summary judgment for entry of one judgment on their claim and another on the counterclaim, but set off one judgment against the other, resulting in a net judgment against petitioners for some \$11,000. The Court of Appeals affirmed. *Held*: The Court of Appeals erred in allowing the setoff, since it thereby granted a preference to the claim of one creditor that happened to owe freight charges over other creditors that did not, and thus interfered with the Reorganization Court's duty under § 77e, 11 U. S. C. § 205 (e), to approve a "fair and equitable plan" that duly recognizes the rights of each class of creditors and stockholders and does not discriminate unfairly in favor of any class. Pp. 2-7.

484 F. 2d 950, reversed.

DOUGLAS, J., wrote the opinion of the Court, in which BURGER, C. J., and BRENNAN, MARSHALL, WHITE, and BLACKMUN, JJ., joined. STEWART, J., filed an opinion concurring in the result, in which POWELL, J., joined. REHNQUIST, J., filed a dissenting opinion.

THE UNITED STATES OF AMERICA

IN SENATE

REPORT OF THE COMMISSIONER OF THE GENERAL LAND OFFICE

FOR THE YEAR 1891

WASHINGTON: GOVERNMENT PRINTING OFFICE: 1892.

1892

1892

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SUPREME COURT OF THE UNITED STATES

No. 73-804

George P. Baker et al.,	}	On Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit.
Petitioners,		
v.		
Gold Seal Liquors, Inc.		

[June 17, 1974]

Opinion of the Court by MR. JUSTICE DOUGLAS, announced by MR. JUSTICE WHITE.

The Penn-Central Transportation Company is in bankruptcy reorganization under § 77, 11 U. S. C. § 205. Petitioners are its trustees authorized to collect its assets, one of which is a claim for freight charges against respondent over the bankrupt debtor. The claim on which this suit was brought was \$8,256.61 and the amount is undisputed. Respondent filed a counter claim for \$19,319.42 for loss and damage to shipments over the debtor's lines. Its amount is also not disputed.

The trustees filed a motion for summary judgment asking the District Court to enter one judgment covering the amount of freight charges admittedly due and another for the amount claimed by respondent.

Previously the Reorganization Court, in the Third Circuit, had prohibited the various bank creditors from offsetting their claims against Trustees for the debtor. 315 F. Supp. 1281. Prior to the decision of the instant case that *Bank Setoff Case* was affirmed by the Court of Appeals, 453 F. 2d 520. Also prior to the ruling of the Court of Appeals in the instant case the Reorganization Court prohibited some shippers from setting off freight loss and damage claims against amounts owed for trans-

portation claims. That order, 339 F. Supp. 603, was affirmed by the Court of Appeals, 477 F. 2d 841, and *sub nom. United Steel Corp. v. Trustees*, — U. S. —.

The District Court in the instant case granted the Trustees motion for summary judgment but set off one judgment against the other, which resulted in a net judgment in favor of respondents against the Trustees in the amount of \$11,017.01. The Court of Appeals affirmed 484 F. 2d, 550; and we granted certiorari to resolve the conflict.

We reverse.

Ordinarily where a court has primary jurisdiction over the parties and over the subject matter, the power to resolve the amount of the claim and the counter claim is clear. Indeed, under the Federal Rules of Civil Procedure the counterclaim may be compulsory. Rule 13 (a).¹ That is the procedure under § 68 of the Bankruptcy Act.²

¹ Rule 13 (a), the compulsory counterclaim rule, requires a defendant to plead any counterclaim which "arises out of the same transaction or occurrence that is the subject matter of the opposing party's claim and does not require for its adjudication the presence of third parties of whom the court cannot acquire jurisdiction." The claim is not compulsory if it was the subject of another pending action at the time the action was commenced, or if the opposing party brought his suit by attachment or other process not resulting in personal jurisdiction but only in rem or quasi in rem jurisdiction. A counterclaim which is compulsory but is not brought is thereafter barred, *e. g.*, *Meaker Brothers Iron Company v. Donata Corp.*, 401 F. 2d 275, 279 (CA4 1968).

If a counterclaim is compulsory, the federal court will have ancillary jurisdiction over it even though ordinarily it would be a matter for a state court, *e. g.*, *Great Lakes Rubber Corp. v. Herbert Cooper Co.*, 286 F. 2d 631 (CA3 1960). Under 13 (a)'s predecessor this Court held that "transaction" is a word of flexible meaning which may comprehend a series of occurrences if they have logical connection, *Moore v. New York Cotton Exchange*, 270 U. S. 593, and this

[Footnote 2 is on p. 3]

The problem of the bankruptcy Reorganization Court is somewhat different. Liquidation is not the objective. Rather the aim is by financial restructuring to put back into operation a going concern.³ That entails two basic considerations:

is the rule generally followed by the lower courts in construing Rule 13A, e. g., *Great Lakes, supra*; *United Artists v. Masterpiece Productions*, 221 F. 2d 213, 216.

Rule 13 (b) permits as counterclaims, although not compulsory, "any claim against an opposing party not arising out of the transaction or occurrence that is the subject matter of the opposing party's claim." Thus the court may dispose of all claims between the parties in one proceeding whether or not they arose in the "same transaction."

² 11 U. S. C. § 106 provides:

"a. In all cases of mutual debts or mutual credits between the estate of a bankrupt and a creditor the account shall be stated and one debt shall be set off against the other, and the balance only shall be allowed or paid.

"b. A set-off or counterclaim shall not be allowed in favor of any debtor of the bankrupt which (1) is not provable against the estate and allowable under subdivision g of section 93 of this title; or (2) was purchased by or transferred to him after the filing of the petition or within four months before such filing, with a view to such use and with knowledge or notice that such bankrupt was insolvent or had committed an act of bankruptcy."

If the trustee in ordinary bankruptcy goes into a court that has jurisdiction and asserts a claim, the debtor of the bankrupt may raise as a set-off any claim he has against the bankrupt and the court ordinarily issues only one judgment for the difference.

In a straight bankruptcy case, *Cumberland Glass Co. v. DeWitt*, 237 U. S. 447, the Court construed § 68 as "permissive rather than mandatory" and as to which the bankruptcy court "exercises its discretion . . . upon the general principles of equity." *Id.*, at 455. And see *Susquehanna Chemical Corporation v. Producer's Bank & Trust*, 174 F. 2d 783.

³ The dissent places mistaken reliance on subsection 1 of § 77 of the Bankruptcy Act, 11 U. S. C. § 205, to argue that the setoff provision of § 68, 11 U. S. C. § 106, necessarily applies to all reorganization proceedings under § 77. No authority is cited for this novel

First is the collection of amounts owed the bankrupt to keep its cash inflow sufficient for operating purposes, at least at the survival level. The second is to design a plan⁴ which creditors⁵ and other claimants will approve, which will pass scrutiny of the Interstate Commerce Com-

struction of subsection 1, and indeed the very wording of the subsection itself makes clear that it applies only when "consistent with the provisions" of § 77. We have long held that the distinctive purposes of § 77 may require different procedures than would be followed in ordinary bankruptcy. For example, in holding that under § 77 the reorganization court had authority to enjoin the sale of collateral if it would hinder or obstruct the preparation of a reorganization plan, we stated: "It may be that in an ordinary bankruptcy proceeding the issue of an injunction in the circumstances here presented would not be sustained. As to that it is not necessary to express an opinion. But a proceeding under § 77 is not an ordinary proceeding in bankruptcy. It is a special proceeding which seeks only to bring about a reorganization, if a satisfactory plan to that end can be devised. And to prevent the attainment of that object is to defeat the very end the accomplishment of which was the sole aim of the section, and thereby render its provisions futile." *Continental Bank v. Rock Island R. Co.*, 294 U. S. 648, 676. And see *New Haven Inclusion Cases*, 399 U. S. 392, 420.

Ordinary bankruptcy aims at liquidation of a business. Reorganization under § 77 aims at a continuation of the old business under a new capital structure that respects the relative priorities of the various claimants.

⁴Section 205 (b) defines a "plan of reorganization." The provisions for filing a "plan" with the Court and with the Interstate Commerce Commission are governed by § 205 (d).

⁵Unsecured creditors have the priority they would have had "if a receiver in equity of the property of the debtor had been appointed by a federal court on the day of the approval" of the bankruptcy petition and shall be treated as a separate class or classes. § 205 (b). As to that priority see *Gregg v. Metropolitan Trust Co.*, 197 U. S. 183. In *St. Louis & S. F. R. Co. v. Spiller*, 274 U. S. 304, 311, the Court said "... by long established practice, the doctrine has been applied only to unpaid expenses incurred within six months prior to the appointment of the receivers The cases in which the time limit was not observed are few in number and exceptional in character."

mission, which will meet the fair and equitable standards required by the Act for Court approval, and which will preserve an ongoing railroad in the public interest."

Section 77 gives the Reorganization Court "exclusive jurisdiction of the debtor and its property wherever located."⁷ 11 U. S. C. § 2052 (a). In furtherance of its long-range responsibilities the Reorganization Court enjoined secured creditors from selling collateral to reduce their claims.⁸ It then went on to bar enforcement of liens against the debtor, taking possession of its property, or obtaining judgments against the debtor, except for specified purposes.⁹ One court seized upon the last pro-

⁷ *New Haven Inclusion Cases*, 399 U. S. 392, 420.

⁸ Section (a) provides in relevant part: "If the petition is so approved, the court in which such order is entered shall, during the pendency of the proceedings under this section and for the purposes thereof, have exclusive jurisdiction of the debtor and its property wherever located, and shall have and may exercise in addition to the powers conferred by this section all the powers, not inconsistent with this section, which a Federal court would have had if it had appointed a receiver in equity of the property of the debtor for any purpose. Process of the court shall extend to and be valid when served in any judicial district."

As Mr. Justice STEWART correctly notes, *infra*, at 2, it is settled that "property" within the meaning of this section includes intangibles such as choses in action.

⁹ The order provided in part: "All persons, firms, and corporations, holding collateral heretofore pledged by the Debtor as security for its notes or obligations or holding for the account of the Debtor deposit balances or credits be and each of them hereby are restrained and enjoined from selling, converting or otherwise disposing of such collateral, deposit balances or other credits, or any part thereof, or from off-setting the same, or any thereof, [sic] against any obligation of the Debtor, until further order of this Court."

¹⁰ "All persons and all firms and corporations, whatsoever and wheresoever situated, located or domiciled, hereby are restrained and enjoined from interfering with, seizing, converting, appropriating, attaching, garnishing, levying upon, or enforcing liens upon, or in any manner whatsoever disturbing any portion or the assets, goods,

vision in the order which says "that suits or claims for damages caused by the operation of trains, buses, or other means of transportation may be filed and prosecuted to judgment in any court of competent jurisdiction," to adjudicate the merits of a counterclaim, but declined to allow the setoff.¹² But proof of the claim against the debtor is a distinct preliminary stage to a determination of what priority, if any, the claim that is proved receives in a reorganization plan.

There is a hierarchy of claims, the owner of the equity coming last. Wages owing workers running the trains have a high current priority. Secured creditors have by law a priority in the hierarchy. Unsecured creditors usually are pooled together. They may receive new securities, perhaps stock. Allowance of a setoff that reduces all or part of the debtor's claim against them is a form of priority. The guiding principle governing priorities is stated in § 205 (e): the Reorganization Court shall approve a plan if it: "[I]s fair and equitable, affords due recognition to the rights of each class of creditors and stockholders, does not discriminate unfairly in favor of any class of creditors or stockholders, and will conform

money, deposit balances, credits, choses in action, interests, railroads, properties or premises belonging to, or in the possession of the Debtor as owner, lessee or otherwise, or from taking possession of or from entering upon, or in any way interfering with the same, or any part thereof, or from interfering in any manner with the operation of said railroads, properties or premises or the carrying on of its business by the Debtor under the order of this Court and from commencing or continuing any proceeding against the Debtor under the order of this Court and from commencing or continuing any proceeding against the Debtor, whether for obtaining or for the enforcement of any judgment or decree or for any other purpose, provided that suits or claims for damages caused by the operation of trains, buses, or other means of transportation may be filed and prosecuted to judgment in any Court of competent jurisdiction. . . ."

¹² *Baker v. Southeastern Michigan Shippers Assn.*, — F. Supp.

to the requirements of the law of the land regarding the participation of the various classes of creditors and stockholders."

The term "fair and equitable" has a long history going back at least to *Northern Pacific R. Co. v. Boyd*, 228 U. S. 482, and *Kansas City Terminal R. Co. v. Central Union Trust Co.*, 271 U. S. 445, whose fixed principle has been carried over into § 77a by our decisions.¹¹ The plan is by terms of § 77 a product of the Interstate Commerce Commission and the Reorganization Court working cooperatively together, *New Haven Inclusion Cases*, 399 U. S. 392, 431. The public interest as well as the interests of creditors and stockholders is at issue.¹² *RFC v. Denver and R. G. W. R. Co.*, 328 U. S. 495, 535.

The allowance or disallowance of setoff may seem but a minor part of the architectural problem. But to the extent that it is allowed, it grants a preference to the claim of one creditor over the others by the happenstance that it owes freight charges that the others do not. That is a form of discrimination to which the policy of § 77 is opposed. As a general rule of administration for § 77 Reorganization Courts, the setoff should not be allowed.¹³

Reversed.

¹¹ *Ecker v. Western Pac. R. Corp.*, 318 U. S. 448, 477-483; *Group of Investors v. Milwaukee R. G.*, 318 U. S. 523, 539-541; *RFC v. Denver & R. G. W. R. Co.*, 516-520. The same is true under § 101 et seq. (now c. X) of the Bankruptcy Act, 11 U. S. C. §§ 501-676. *Consolidated Rock Products v. Du Bois*, 312 U. S. 510.

¹² And see *New Haven Inclusion Cases*, 399 U. S. 392, 420.

¹³ *Lowden v. Northwestern National Bank and Trust Co.*, 298 U. S. 160 is not to the contrary. The Court there refused to answer the certified question because it did not know the factual setting in which the question had been raised. Much law has been fashioned in the reorganization field since 1936, the date of that decision. The contours of plans have emerged which have given new meaning and insight into the statutory words "fair and equitable." The preference sought here shows no exceptional circumstances which in equity justify the discrimination.

SUPREME COURT OF THE UNITED STATES

No. 73-804

George P. Baker et al., } On Writ of Certiorari to the
Petitioners, } United States Court of
v. } Appeals for the Seventh
Gold Seal Liquors, Inc. } Circuit.

[June 17, 1974]

MR. JUSTICE STEWART, with whom MR. JUSTICE POWELL joins, concurring in the result.

The Court concludes that since the allowance of a setoff in a § 77 reorganization would grant "a preference to the claim of one creditor over the others by the happenstance that it owes freight charges that the others do not," such setoffs should be disallowed "[a]s a general rule of administration." *Ante*, pp. 6-7. While I agree that the District Court should not have permitted a setoff in this case, I think that the broad rule adopted by the Court is unnecessary to reach this result, and I prefer to rest my conclusion on a narrower ground.

While judicial setoffs are specifically authorized in straight bankruptcy cases, § 68, 11 U. S. C. § 108, no express approval of them appears in the statute governing § 77 reorganizations.¹ In *Lowden v. Northwestern*

¹ I am unable to conclude, as does the dissent, *post*, at 2-3, that subsection *l* of § 77 mandates allowance in § 77 reorganizations of all setoffs allowed by § 68 in straight bankruptcies. While the dissent's ingenious reading of the statute would provide an easy semantic solution to the problem presented in this case, I am impressed with the fact that neither this Court in *Lowden v. Northwestern National Bank & Trust Co.*, 298 U. S. 160 (1936), nor, apparently, any other federal trial or appellate court has considered subsection *l* to have any bearing whatsoever on the setoff problem. In the absence of any showing based on legislative history that

National Bank & Trust Co., 298 U. S. 160 (1936), this Court stated that the approval of setoffs in § 68 did not control in railroad reorganizations but "governs, if at all, by indirection and analogy according to the circumstances. The rule to be accepted for the purpose of such a suit is that enforced by courts of equity, which differs from the rule in bankruptcy chiefly in its greater flexibility, the rule in bankruptcy being framed in adaptation to standardized conditions, and that in equity varying with the needs of the occasion, though remaining constant, like the statute, in the absence of deflecting forces." *Id.*, at 164-165.²

By announcing a doctrine barring judicial setoffs as "a general rule" the Court in the present case adopts a rationale inconsistent with *Lowden*, which quite clearly envisioned a case-by-case analysis of the propriety of each attempted setoff in the light of equitable considerations. Rather than replacing this principle with a new and wholly inconsistent rule to be applied in all cases involving judicial setoffs, I would rest this decision on

such was the intent of Congress, and particularly in the absence of any briefing or oral argument on the matter, I would not, therefore, give this less than pellucid provision the force ascribed to it by the dissenting opinion.

² These statements of the Court concerning allowance of judicial setoffs in § 77 cases were, in a technical sense, dicta. The *Lowden* case came to the Court on questions certified by the Court of Appeals for the Eighth Circuit, and the Court dismissed the certificate without formally answering the questions because of the "defective form of the certificate . . ." 298 U. S. 160, 166. The Court's reasoning as to the availability of setoffs, however, has been viewed as authoritative. See, e. g., *In re Lehigh & Hudson River Railway Co.*, 468 F. 2d 430, 433 (CA2 1972); *In re Yale Express System*, 362 F. 2d 111, 116-117 (CA2 1962); *Susquehanna Chemical Corp. v. Producers Bank & Trust Co.*, 174 F. 2d 783, 787 (CA3 1967). See also 4 Collier, Bankruptcy ¶ 68.10 [2], at 898-900, n. 17 (1971).

the particular facts before us, which adequately distinguish this case from the situation in *Lowden*.²

Section 77 gives the Reorganization Court "exclusive jurisdiction of the debtor and its property wherever located." (Emphasis added.) It has been commonly accepted in the federal courts that "property" within the meaning of this section includes intangibles such as choses in action. See 2 Collier, *Bankruptcy* ¶ 23.05 [4], at 485 (1971), and cases there cited. It follows, therefore, that the respondent's debt to the Penn Central fell within the "exclusive jurisdiction" of the Reorganization Court immediately upon the approval of the petition for reorganization. While such jurisdiction may not empower the Reorganization Court to enforce the cause of action, see *id.*, at 489-490; *In re Roman*, 23 F. 2d 556 (CA2 1928) (L. Hand, J.), it certainly does empower the court to protect the "property" and to immunize it from diminution through setoff or counterclaim. To hold otherwise would be inconsistent with the function of the Reorganization Court to consolidate and protect the assets of the petitioning corporation. *Callway v. Benton*, 336 U. S. 132, 147 (1949); *Warren v. Palmer*, 310 U. S. 132, 139-141 (1940); *Ex parte Baldwin*, 291 U. S. 610, 615 (1934).

While the matter is not wholly free from doubt, I am persuaded that the Reorganization Court in this proceeding did in fact enjoin the allowance by any other court of judicial setoffs against any debts owed to the

² Because of my view of this case I need not comment on the propriety of the rule adopted by the Court, although I think there are strong arguments that the rule can be unfair, see, e. g., *In re Lehigh & Hudson River Railway Co.*, *supra*, 468 F. 2d, at 434, and that those arguments are not dealt with in the Court's opinion today.

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Penn Central.⁴ On this basis I join the judgment of the Court.

⁴The Reorganization Court's initial order approving the Penn Central's petition for reorganization, filed on June 21, 1970, contained the following provisions:

"9. All persons and all firms and corporations, whatsoever and wheresoever situated, located or domiciled, hereby are restrained and enjoined from interfering with, seizing, converting, appropriating, attaching, garnisheeing, levying upon, or enforcing liens upon, or in any manner whatsoever disturbing any portion of the assets, goods, money, deposit balances, credits, choses in action, interests, railroads, properties or premises belonging to, or in the possession of the Debtor as owner, lessee or otherwise, or from taking possession of or from entering upon, or in any way interfering with the same, or any part thereof, or from interfering in any manner with the operation of said railroads, properties or premises or the carrying on of its business by the Debtor under the order of this Court and from commencing or continuing any proceeding against the Debtor, whether for obtaining or for the enforcement of any judgment or decree or for any other purpose, provided that suits or claims for damages caused by the operation of trains, buses, or other means of transportation may be filed and prosecuted to judgment in any Court of competent jurisdiction, and provided, further, that the title of any owner, whether as trustee or otherwise, to rolling stock equipment leased or conditionally sold to the Debtor, and any right of such owner to take possession of such property in compliance with the provisions of any such lease or conditional sale contract, shall not be affected by the provisions of this order.

"10. All persons, firms and corporations, holding collateral heretofore pledged by the Debtor as security for its notes or obligations or holding for the account of the Debtor deposit balances or credits be and each of them hereby are restrained and enjoined from selling, converting or otherwise disposing of such collateral, deposit balances or other credits, or any part thereof, or from offsetting the same, or any thereof, against any obligation of the Debtor, until further order of this Court."

SUPREME COURT OF THE UNITED STATES

No. 73-804

George P. Baker et al.,	} On Writ of Certiorari to the
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v.	
Gold Seal Liquors, Inc.	} United States Court of Appeals for the Seventh Circuit.

[June 17, 1974]

MR. JUSTICE REHNQUIST, dissenting.

The question in this case is whether the United States District Court for the Northern District of Illinois, wherein petitioners filed their claim for money damages against respondent, and the Court of Appeals for the Seventh Circuit, which affirmed the District Court's order setting off respondent's claim against petitioners, acted within the permissible limits of their discretion. The statute most closely in point is § 68 of the Bankruptcy Act, 11 U. S. C. § 108, which provides:

"(a) In all cases of mutual debts or mutual credits between the estate of a bankrupt and a creditor the account shall be stated and one debt shall be set off against the other, and the balance only shall be allowed or paid."

In the only case of this Court dealing with the applicability of § 68 to railroad reorganizations, the Court said:

"... [T]he trustees must have the power to gather in the assets and keep the business going. To exercise that power, they may find it necessary to sue, and the suit may turn upon the right of set-off, as it does in the case at hand. In a suit for such a purpose, a suit collateral to the main proceeding and initiated at a time when the outcome of that pro-

ceeding is still unknown and unknowable, § 68 of the statute does not control *ex proprio vigore*. It governs, if at all, by indirection and analogy according to the circumstances." *Lowden v. Northwestern National Bank & Trust Co.*, 298 U. S. 160, 164 (1936).

"When all the facts are known, they may be found to offer no excuse for a departure from the rule in bankruptcy which, as indicated already, is generally, even if not always, the rule in equity as well." *Id.*, at 166.

The Court's opinion in *Lowden*, *supra*, makes no mention of subsection (1) of section 77 of the Bankruptcy Act, 11 U. S. C. § 205, which provides in pertinent part as follows:

"(1) *Jurisdiction of court, duties of debtor and right of creditors same as in voluntary bankruptcy.*

"In proceedings under this section and consistent with the provisions thereof, the jurisdiction and powers of the court, the duties of the debtor and the rights and liabilities of creditors, and of all persons with respect to the debtor and his property, shall be the same as if a voluntary petition for adjudication had been entered on the day when the debtor's petition was filed."

Section 77, in turn, was a part of the Act of March 3, 1933, ch. 204, 47 Stat. 1467, which added Chapter VIII to the Bankruptcy Act. Any lingering doubt that the term "voluntary petition for adjudication" in subsection (1) refers to ordinary bankruptcy proceedings is dispelled by an examination of § 73, which was the first section of that Act:

"Sec. 73. *Additional Jurisdiction.* In addition to the jurisdiction exercised in voluntary and involun-

tary proceedings to adjudge persons bankrupt, courts of bankruptcy shall exercise original jurisdiction in proceedings for the relief of debtors, as provided in sections 74, 75, and 77 of this Act." 47 Stat. 1467.

The language of subsection (1) of § 77, even more emphatically than the *Lowden* decision, would seem to unconditionally mandate the application of the rule regarding setoffs contained in § 68 of the Bankruptcy Act to railroad reorganizations such as this.

Subsection (a) of § 77, 11 U. S. C. § 205 (a), giving the Reorganization Court "exclusive jurisdiction of the debtor and its property wherever located," upon which the Court's opinion heavily relies, seems to me to have virtually nothing to do with this case. We are not dealing with property that was actually or constructively in the possession of the trustees at the time of the commencement of the reorganization proceedings, nor are we dealing with a creditor who in any way submitted himself to the jurisdiction of the Reorganization Court in the Eastern District of Pennsylvania.

This is a simple contract claim for freight charges on the part of the trustees, against which the respondent has sought to set off a concededly valid claim for damage in transit. While the Reorganization Court undoubtedly had plenary authority over the trustees, and of the "property" of the debtor, it certainly does not have such jurisdiction over whatever funds of respondent might be used to satisfy a judgment against him in favor of the trustees. The trustees' "property" in this case is a chose in action and under no conceivable circumstances could § 77 authorize the summary determination of the claim in this case.

"The Bankruptcy Court does not have summary jurisdiction to enforce a chose in action against a bankrupt's obligor, even when the bankrupt's rights

seem clear" *In re Lehigh and Hudson River Railway Co.*, 468 F. 2d 430, 433 (CA2 1972) (Friendly, J.).

"Even though [the obligor's] refusal were no better than colorable, its property remained its own; it had only broken its promise, and like any other promisor, was liable to an action for damages It would not be permissible to collect even a bank deposit due a bankrupt by these means." *In re Roman*, 23 F. 2d 556, 558 (CA2 1928) (L. Hand, J.).

Cases such as *Ex parte Baldwin*, 291 U. S. 610 (1934), and *Warren v. Palmer*, 310 U. S. 132 (1940), do no more than reaffirm the well-established doctrine that the jurisdiction of the bankruptcy court over the property of the debtor is exclusive. They do not touch upon the case before us, where the trustees have chosen to convert the chose in action, which is concededly the property of the debtor and subject to the jurisdiction of the reorganization court, into a money judgment in another forum.

Callaway v. Benton, 336 U. S. 132 (1949), though not on all fours with the present case, can hardly be said to support the result reached by the Court. There an action had been brought in the state courts of Georgia to enjoin the Board of Directors of a corporation which had leased trackage to the Central of Georgia Railway from consenting to the plan of reorganization which had been proposed on behalf of Central of Georgia, which was a debtor in a Chapter 77 proceeding. The bankruptcy court had in turn enjoined this litigation on the ground that it interfered with the exclusive jurisdiction of the bankruptcy court. This Court reversed that determination saying:

"We have held that a court of bankruptcy has exclusive and nondelegable control over the administration of an estate in its possession. *Thompson v. Magno-*

lia Petroleum Co., 309 U. S. 478 (1940); *Isaacs v. Hobbs Tie & T. Co.*, 282 U. S. 734 (1931). There can be no question, however, that Congress did not give the bankruptcy court exclusive jurisdiction over all controversies that in some way affect the debtor's estate." 336 U. S., at 142.

If we accept *Lowden* as the final word from this Court on the question, even though the opinion nowhere refers to the language of subsection (1) which on its face would carry over the rule of § 68 bag and baggage, the most that can be said in favor of the petitioners here is that the District Court in which suit is brought had discretion as to whether or not a setoff should be allowed.

Nothing could be more inconsistent with *Lowden* than the flat order of the Reorganization Court in this case, entered at the commencement of the reorganization proceedings, to the effect that no setoffs were to be allowed, unless it be that part of the Court's opinion in this case stating that "[a]s a general rule of administration for § 77 Reorganization Courts, the setoff should not be allowed." *Ante*, at 7. And it seems a sufficient answer to the Court's observation that the allowance of a setoff grants a preference, *ante*, at 6, to say that the Bankruptcy Act's strictures against preferences apply with as much force to ordinary bankruptcies as to reorganizations, and yet § 68 of the Act specifically allows this type of "preference" in an ordinary bankruptcy proceeding.

It may be that upon a proper showing to the District Court for the Northern District of Illinois the trustees could have satisfied that court that the allowance of a setoff in this case would be inconsistent with higher priorities of the reorganization. But no such showing was made by the trustees, and they were content to rely on the *ex parte* order of the Reorganization Court which

made no pretense of considering matters on a case-by-case basis. The District Court for the Northern District of Illinois was, therefore, in my opinion, justified in authorizing the setoff under the doctrine of *Lowden*, and the Court of Appeals for the Seventh Circuit was correct in affirming its judgment.

